



Fraud:

Reducing the risks in your charity

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What is fraud?

Fraud is a crime in which some kind of deception is used for personal gain. Fraud comes in many forms and anyone can be a target, including charities.

Fraud can be **internal**, committed by someone within your charity, or **external**, committed by someone not directly involved in the charity.

If you think your charity has been a victim of fraud you should report it to Police Scotland by phoning 101 immediately. You also need to tell OSCR by sending us a **notifiable event**.

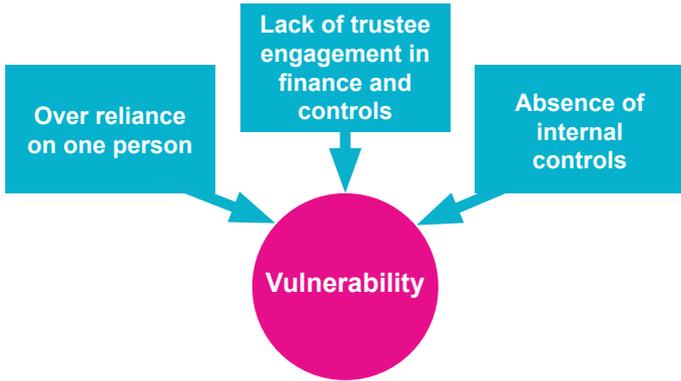
Internal fraud

The vast majority of people involved in charities are honest; however, like other sectors charities are not immune from internal or insider fraud. Examples of internal fraud can include:

- Setting up payments to a fake supplier
- Making payments to an employee who does not exist
- Making overpayments for services or products
- Unauthorised access being gained to the charity's bank account leading to inappropriate payments being made.

Research from a Charity Commission for England and Wales study **Focus on insider fraud: research report** concludes that much of the insider fraud looked at in the study were made possible by the organisational culture within the charity, that put too much trust and responsibility in one individual, or allowed a lack of challenge and oversight.

Having an organisational culture which values openness and transparency can help to overcome these vulnerabilities.



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Charity trustee duties and fraud prevention

As a charity trustee, you have a duty under the **Charities and Trustee Investment(Scotland) Act 2005 (the 2005 Act)**, to act in the interest of their charity and in particular to act with the care and diligence that it is reasonable to expect of a person who is managing the affairs of another person.

This means that you must act with a higher level of care than you do with your own finances and affairs. You must make sure that you protect the charity's resources and that you do not put the assets of the charity at risk.

Charity trustees should:

- understand where their charity is vulnerable to fraud
- effectively manage identified risks.

Charity trustees are responsible for the prevention and detection of fraud, even if they delegate some of their executive responsibilities to individual trustees, senior staff or volunteers. Charity trustees have a collective responsibility for financial records and controls over financial procedures to protect the assets of the charity. Ultimately, charity trustees are accountable for all that happens within their charity.

The risk from financial fraud and abuse can never be completely ruled out. However proper and adequate internal financial controls play an important part in managing these risks.

Charity trustees should:

- identify the risks they face from fraud, assessing any particular vulnerability
- document these risks and any changes over time
- manage and/or mitigate these risks
- consider mitigation measures as part of the routine governance of the charity
- pay attention to fundraising, as a point of engagement with the public.

Where charities give large amounts of money to partners and beneficiaries then they must make sure that adequate monitoring takes place – this means verifying that charity funds or property reaches the proper destinations and are used how the charity intended.

a) Developing an Anti-Fraud Policy

An Anti-Fraud policy should be appropriate and proportionate to the size and scale of your charity. The activities your charity carries out will play a part in shaping your policy.

The policy should encourage reporting of anything suspicious, and get all staff to communicate any irregular events or incidents. The policy should be straight forward and easy to understand so staff, volunteers and charity trustees feel confident about what and when to report and what action to take.

Remember: charity trustees are the guardians of donated funds and public money.

Things to think about when developing an Anti-fraud policy:

- **Introduction** – who does this policy apply to, what kind of action will be taken if fraud is identified or suspected.
- **Definition of fraud** – include any particular areas of vulnerability identified in the risk assessment/management process.
- **Responsibilities** – specify the different strategic and operational responsibilities undertaken by charity trustees, chief officer, senior managers, staff and volunteers in preventing and responding to fraud.
- **Other relevant policies** – recruitment (employee references) whistleblowing, financial procedures manual, risk register.

- **Detection and investigation** – is there a designated staff member or charity trustee with responsibility for investigating fraud? If this person falls under suspicion, who will investigate?
- **Disciplinary procedures** – are there any circumstances which may lead to disciplinary action? For example, failing to follow internal controls and financial procedures, making malicious accusations.
- **Reporting** – to whom will cases of suspected or actual fraud be referred? In what circumstances?
- **Review and refresh** – make sure your policy is reviewed and updated as necessary, and appropriate training is provided.

Charity trustees need to take the risk of fraud seriously and act to protect the charity, including its assets and reputation.

b) Internal financial controls

One way of following the duty to act with care and diligence is to make sure that there are proper financial controls in place.

What do we mean by financial controls?

Good financial controls are tools for making sure that you manage the charity effectively and meet your legal duty to act with care and diligence.

Financial controls are the systems you have in place to make sure that you protect the assets of the charity.

Reviewing accounts

A major part of financial control is to review the accounts. A useful way to do this is to compare the amounts spent on individual expense categories since they were last reviewed with what was expected to be spent in that period. Ideally, a budget will be prepared and approved by the charity

trustee board before the beginning of the financial year. Then the actual results can be compared to the expected or budgeted results, making it easier to investigate any differences or 'variances'.

In a small organisation it may be appropriate just to compare the expenditure of one period with that of the corresponding previous period, for example the month before.

Controls offer protection

It is important to remember that being a charity trustee is a significant responsibility. Where controls are correctly set up and used they will both protect the assets of the charity and you as a charity trustee.

What areas do you need to consider?

• Collective responsibility

All of the charity trustees have responsibility for the financial records, not just the treasurer. As charity trustees, it is important that you all have a basic understanding of the finances of your charity and can quickly identify if there are any problems. The financial information should be discussed at meetings to make sure that everyone knows the charity's financial situation. For example, finance should be a recurring item on the agenda of every board meeting. It is good practice that someone other than the treasurer also has an understanding of how the charity's financial records are kept.

• Finance Committee

Some organisations find it helpful to set up a finance sub-committee of charity trustees and advisors with financial or accounting knowledge. They have additional meetings to spend extra time on detailed finance matters, like budget preparation, and then report back to the charity trustee board. Having a committee does not absolve the other charity trustees of their collective responsibility but can be helpful in clarifying matters that are

submitted to the full charity trustee board.

• Separation of duties

Where possible you should separate out the administrative tasks so that no one individual has sole responsibility for the financial transactions of your charity. We call this 'separation of duties'.

For example, when your charity makes a purchase the same individual (whether it is a charity trustee, employee or volunteer) should not be responsible for arranging the purchase, authorising the payment and making the payment. In very small charities, it can be difficult to have a separation of duties. You should make sure that checks are regularly carried out on financial records and transactions to compensate for this.

• Written procedures

Your financial procedures should be documented. This will help where charity trustees change regularly and if something unexpected happens such as a treasurer being taken ill.

You should review your procedures annually to make sure they are still fit for purpose, being followed correctly and understood.

• Controls over cash

Where possible it is best to avoid the use of cash, as it is harder to maintain a trail of cash and much easier for theft or fraud to happen and go undetected. You should encourage donations to be made by bank transfer, cheques or online and you should make payments in this way wherever possible.

If you do receive cash donations, two people should count these and then make sure the money is banked as soon as possible. You should issue receipts for the donations and not make any payments out of this cash before taking it to the bank.

You should keep petty cash to a minimum. Receipts should be required for all items of petty cash. Access to the petty cash box should be restricted and it should be held in a secure place. A cashbook should be kept to record what goes into the petty cash and what is paid out of it. Each time there is money added to or taken out of the petty cash it should be recorded in the cash book with supporting documentation, such as a copy of a donation receipt or expenditure receipt. The amount in the petty cash box should be regularly counted and compared to the balance in the cashbook to make sure that all money is properly recorded and accounted for.

• Banking

Banking is an important part of the financial controls. Charity trustees have a legal duty to protect the charity's assets and so should make use of regulated banking services where these are available to make sure the charity's funds are secure. When considering your charity's banking arrangements, you should choose an organisation that is able to offer formal banking facilities and the full range of services that you need. In the UK those organisations that are able to offer formal banking facilities are usually authorised and regulated by the Financial Conduct Authority (FCA).

Banks will ask for details of all signatories and usually all the charity trustees, so be prepared to have this information available. You should be aware of the terms and conditions of your banking arrangements and advise the bank immediately of any changes that may affect these for example, a change of signatories.

Bank statements should be agreed to the accounting records regularly, at least monthly, and someone other than the person who is otherwise involved in the banking process should review these reconciliations.

Bank reconciliations should be reviewed at trustee meetings. In smaller charities, bank statements and transactions may be checked at trustee meetings.

• Cheque payments

Cheques should have a minimum of two signatories to make sure that it is not just one person who can make payments. You should have systems in place to check invoices and authorise payments before they are made.

You should not sign cheques where the amount and the recipient are not already filled in (blank cheques). You should ensure that the details on the cheque stub match the corresponding cheque. If this is not done the cheques may not be accounted for correctly and might result in lost or stolen money.

• Automated payments

Automated payments from the bank account such as Direct Debits and Standing Orders should be subject to the same controls as other payments. A review of all such automated expenditure should take place regularly.

• Internet banking and online payments

It can be more difficult to develop tight financial controls for bank transfers as access may be restricted to a single log in. You should consider making a rule that two people have to be present when large transactions are being processed.

Some banks allow charities to provide more than one person to authorise payments (dual authority). You should ask your charity's bank for details of their dual authority options so that you can consider what is right for your charity.

• Credit Cards

Credit cards are often required to pay for travel or purchase items online. There should be internal control procedures to cover this including credit limits, authorisation procedures and review and authorisation of credit card statements.

How OSCR looks at fraud

OSCR's role is to make sure that charities comply with the requirements of Scottish charity law and that charity trustees run charities in line with their legal duties.

Where fraud occurs in a charity, our focus is to make sure that charity trustees act appropriately and in accordance with their charity trustee duties. We look to see whether you have suitable controls over financial procedures to protect the assets of the charity and what steps the charity trustees have taken since the event happened to ensure it doesn't recur.

If you fail to comply with the charity trustee duties then this is misconduct and we do have powers to take action, where appropriate. Our response will be proportionate depending on the situation. Where a charity trustee has acted reasonably and honestly it is unlikely to be treated as **misconduct**.

You can find out more about what we can and cannot do and what to expect if we have a concern about your charity on [our website](#).

OSCR is not responsible for investigating or prosecuting criminal activity. Where we have concerns regarding criminal conduct we can and do report them to the Crown Office and Procurator Fiscal Service.

Our **Inquiry Policy** sets out how we assess concerns about charities. The policy sets out the matters that OSCR can and cannot deal with and explains how we assess concerns to decide if we take them forward.

Where a fraud is identified within a charity, the charity trustees should first of all report this to the police.

Reporting instances of fraud to OSCR

Our Notifiable Events regime requires charity trustees to report events that are likely to have a significant impact on their charity. When there has been a fraud, charity trustees should consider our **Guidance on Notifiable Events** to understand whether this should also be reported to us.



Reporting demonstrates that charity trustees have identified a serious incident within their charity and that they are taking appropriate action to deal with it and protect the charity from further risk or abuse.

When reporting, trustees should provide as much information as possible about the facts of the case and the actions being taken. This will allow us to assess if the appropriate actions are being taken in any given case.

There is no legal requirement to report a notifiable event. However, it is an important way for charity trustees to reassure us that they are on top of the issues they are facing. Ultimately, we may become concerned if there has been a matter that has not been reported to us; especially if it goes on to have a negative impact on the individual charity or the wider charity sector. Where something significant has happened within a charity and this has not been reported to us in full, we will take this into account if we have to open an inquiry. Ultimately, this could be considered to be misconduct.

Reporting a notifiable event helps OSCR to assess the volume and impact of fraud incidents within charities and to understand the risks facing the sector as a whole. This helps us to decide how we can better support charities through our guidance and assess where we need to focus our activities.

If you're not sure whether to report something as a notifiable event please **contact us**.

Where can I get more information?

- The **Action Fraud website** contains more detailed information on fraud and how to protect yourself.
- The **Charity Finance Group has guidance and checklists** designed for small charities looking to prevent fraud.
- The Charity Commission for England and Wales has guidance called '**Protect your charity from fraud**' and **Internal financial controls for charities (CC8)** which contains practical advice and links to other sources of help.
- OSCR's factsheet: **Cybercrime - what is it and what you need to know.**

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