



# Breach of Trust

An investigation into  
the incidence, origins and  
impact of fraud in the  
charitable sector

A REPORT BY THE FRAUD ADVISORY PANEL

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Fraud is not a word commonly associated with the charitable sector. But altruism, trust and goodwill are; they describe the beating heart of charitable work, wherever it is performed. But might these traditional strengths also contain the seeds of a particular vulnerability to fraud?

There is certainly a perception that the charitable sector's altruistic nature makes it a 'soft target' for the unscrupulous. But in reality much of what we think we know comes from anecdotal evidence and a few headline cases in the media. When it comes to measuring the incidence of fraud among charities, even informed estimates vary widely.

Using self-completion questionnaires, followed up with a series of in-depth interviews, this survey set out to:

- investigate charities' attitudes to fraud;
- explore anti-fraud strategies and whether these are a match for the threats;
- measure the incidence, size and nature of the frauds committed; and,
- explore whether charities of different types and sizes also experience fraud and its consequences in different ways.

Our findings reveal that even though reported fraud is still less common among charities than in mainstream business, the impact on individual organisations and the sector as a whole can be devastating. Those that fall victim to fraud must cope not only with direct financial losses but also cancelled projects, damaged reputations, adverse publicity and, perhaps most distressingly, the undermining of that special commitment and team spirit that so often bridges the gap between what a charity can afford in strict accounting terms, and what it achieves in human terms.

These are serious threats – severe enough, we are told, to have taken some charities to the very brink of closure. And yet our survey also reveals that many charities (and especially the smaller ones) still have no serious anti-fraud measures or training programmes in place.

There is, it seems, a widespread assumption that fraud is something that happens only to someone else. To overcome this inertia is, then, an immediate challenge. We very much hope that this survey will help all charities to become more aware of how severely fraud can hurt them, as well as to explore urgently how they might best protect themselves and those who depend on their continuing good work.

*The Fraud Advisory Panel would like to acknowledge the invaluable support of our sponsors, Chantrey Vellacott DFK LLP, and would also like to thank all of the charities that took the time to complete the survey and especially those who participated in the case study interviews.*

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# Key Findings

## Perceptions of vulnerability

- Half of all respondents think fraud is a major risk to the charity sector.
- A quarter think it is a bigger risk to the charity sector than to other sectors.
- Charities believe themselves to be vulnerable because unethical people exploit the sector's presumption of trust and goodwill.
- A quarter think their charity is most vulnerable to fraud by staff or volunteers.

## Risk management

- Two-thirds of respondents (but almost 90% of very large charities) have designated one or more people to be responsible for fraud prevention. Typically this is the chief executive, finance director or a trustee.
- But 60% of respondents have no anti-fraud policies and procedures in place at all.
- The other 40% are most likely to have a whistleblowing policy (18%), fidelity or crime protection insurance (16%) and/or a risk register that includes fraud (14%).
- Only 11% have an anti-fraud policy, and 14% of those do not systematically communicate it to staff.

## Scale and incidence

- Overall, 7% of respondents have been the victim of fraud within the last two years.
- Half of them estimate their total direct financial loss at less than £1000; just 2% report losses of more than £100,000.
- Fraud is significantly more common among the largest charities (20%), those that employ full-time staff (15%) and those with trading subsidiaries (20%). The presence of volunteer workers makes no difference to the incidence of fraud.

## How it happens

- Most frauds take place at head office (18%) or within the banking system (17%) and involve the theft of cash (28%) or cheques (23%).
- Almost half of all victims knew who committed their fraud. Typically it was a paid employee acting alone.
- But a fifth don't know where the fraud took place and a quarter don't know for how long it had been going on.
- Frauds are most often discovered by internal controls or audits (46%) or by the bank (18%).

## Impact

- A quarter of victims report some negative impact on their organisation, mostly reputational damage or an inability to fund specific projects.
- The in-depth interviews reveal significant damage to staff morale and well-being, with some staff suffering stress, feelings of betrayal, illness and redundancy.

## Response

- The vast majority (83%) of victims reported the fraud to their board of trustees. Three-quarters also reported it externally, typically to the police or the bank, but not to the Charity Commission (just 10%).
- Where the identity of the fraudster was known, two-thirds of victims took action against the individual – mostly by involving the police (33%) or by dismissal (22%). About a quarter took no action at all or didn't know what action had been taken.
- Half recovered some or all of their money.
- Half felt that, in retrospect, they had contributed in some way to the fraud taking place, generally by being too trusting or by operating inadequate risk management systems.

*The full report, including graphical presentations of the detailed findings, can be downloaded from our website at: <http://www.fraudadvisorypanel.org/>*

*Select the 'Publications' tab and then 'Research'.*

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## Methodology

The study was conducted in two phases during the fourth quarter of 2008.

A self-completion postal survey was sent to a sample of 5000 registered charities in England and Wales drawn randomly from the Charity Commission's register. To enable size comparisons the register was stratified into four income bands and a random sample taken from each. A total of 1123 responses gave a 22% response rate (good for a survey of this type) and came mostly from office holders: treasurers (19%), chief executives (15%), chairmen (13%), secretaries or company secretaries (10%), finance directors (9%), trustees (8%).

The second phase was a series of in-depth interviews with six charities that had reported a fraud in the first phase. These organisations were selected so as to create a representative cross-section in terms of size, activity and the type of fraud suffered.

**"On a day-to-day basis we're dealing with really quite a lot of cash and there is always the possibility of – I wouldn't call it fraud – pilfering"**

## Are charities particularly vulnerable to fraud?

Half of all respondents agreed with the assertion that fraud is a major risk to charities, and a quarter agreed that fraud is a greater risk to the charity sector than to other sectors. Charities that have been victims of fraud are more likely to agree with both assertions (64% and 41%, respectively).

The main reason given for this perceived vulnerability is the sector's reliance on goodwill and trust which can, it is thought, allow unethical people (which may include staff and volunteers) to take advantage. Others included:

- lower levels of management expertise or financial control;
- less frequent or rigorous staff training;
- unsupervised fundraising by the general public; and,
- too trusting an approach to colleagues and volunteers, and insufficient checks and division of responsibilities in financial matters.



When asked to identify the area within their organisation most vulnerable to fraud, respondents said: staff and volunteers (25%), fundraising events (18%), contractors and suppliers (11%), beneficiaries (10%), public collections (8%) and donations (8%).

## Scale and incidence

In fact the incidence and cost of fraud among charities remains low by the standards of mainstream commerce. Just 7% of all respondents reported that their organisations have been the victim of fraud within the last two years (against something like a half for businesses as a whole). Half of all the reported frauds involved losses of less than £1000, with only a small minority (2%) exceeding £100,000.

Frauds against charities are most likely to have taken place in the organisation's head office (18%) or within the banking system (17%). The most common types of fraud are the theft of cash (28%) or cheques (23%), followed by theft of inventory (10%), credit card fraud (8%) and identity fraud (7%). Theft of cash is most common amongst charities with paid employees (34% compared with 4% among organisations with no paid staff).

The respondents who know who committed their fraud (ie, half of all victims) reported the following typical characteristics:

- gender: male (44%); female (49%).
- age: 20–29 years (31%); 30–59 years (39%).
- relationship to the charity: paid employee (40%); volunteer (11%); contractor (7%); none (11%).

**"...up to now I'd never have put the day care centre and fraud in the same box."**

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## Impact

The impact of fraud is keenly felt in a sector where even small amounts count. Among charities that have experienced a fraud, a quarter reported some negative consequence for the organisation, reputational damage (12%) and an inability to fund specific projects (10%) being the most common. Adverse media publicity (8%) and limitations on the charity's range of activities (7%) were also mentioned.

Damage to specific projects hurts the smaller charities most (18% versus none for the larger charities). Larger charities are more likely to lose volunteers and/or staff (10% compared to none for the smaller organisations).

In-depth interviews shed further light here, especially on the potential impact on staff morale. More than one interviewee commented that those working in the charitable sector do so out of commitment rather than for financial reward; they expect colleagues to maintain the same high standards that they expect of themselves, and are bitterly upset if their expectations prove unfounded.

- One organisation lost contracts as a result of a fraud and then had to make staff redundant, creating high levels of workplace stress from which several employees became ill.
- Elsewhere, colleagues found it hard to accept that a friend and board trustee had let them all down.
- In another charity, first everyone felt under suspicion when money was taken from the accounts of residents with learning disabilities, then this gave way to feelings of disbelief and betrayal that a valued colleague could have behaved in such a way.

**"...we were two weeks away from going down [financially] basically – that's how close it was."**

## Risk factors

The likelihood of fraud is highest among the largest charities (20% have experienced fraud versus 7% overall), those that employ full-time staff (15% compared to 3% for organisations that have no full-time paid staff) and those with trading subsidiaries (20%).

Charities which sponsor or undertake research (15%), provide advocacy, advice and information (13%), or provide other finance (13%) are approximately twice as likely to experience fraud. No difference was found based solely on whether or not an organisation uses volunteer workers.

## Fraud prevention

Just over two-thirds of charities (68%) reported that one or more people are specifically responsible for fraud prevention in their organisation, and this proportion increases markedly with the size of charity: 62% of the smallest; 88% of the very largest. Senior management roles are the most likely to be nominated.

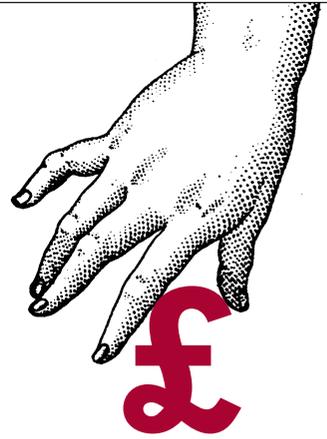
And yet 60% also said that they have implemented none of the suggested anti-fraud measures<sup>1</sup>. Even among those who have experienced fraud, half have none of the suggested measures in place. There are very significant differences in this respect according to the size of the charity. Almost three-quarters of the smallest charities (73%) have no anti-fraud measures in place, compared with 14% of the very largest.

**"The main thing is internal control; that's what was totally lacking...they [the charity] put their trust in one person [the Treasurer] and nobody ever checked on what he was doing or how he was doing it....A lot of charities are in the same boat; it's all a question of trust."**

Of the 40% with one or more measures in place, these are most likely to be a whistleblowing policy (18%), fidelity or crime protection insurance (16%) and/or a risk register that includes fraud (14%). Significantly fewer charities reported having an anti-money laundering policy (8%) or a fraud response plan (4%).

Overall, just 11% of respondents (generally larger charities) have an anti-fraud policy, but most of these (86%) do communicate it to their staff, volunteers and trustees. This is most commonly done through departmental or team meetings (40%) or as part of the induction programme for new employees (30%). Some charities also make their anti-fraud policy available on their intranet (14%) or include it as part of a continuing training scheme (14%).

<sup>1</sup> Anti-fraud policy, anti-money laundering policy, whistleblowing policy, fidelity or crime protection insurance, fraud awareness training programme, fraud response plan, and a risk register that includes fraud.



## The response

The majority of those charities that have fallen victim to fraud did report the crime to their Board of Trustees (83%) and at least one external body (75%), typically the police (51%) and/or their bank (36%).

But that leaves almost a quarter (24%) who did not report it, not even to the Charity Commission. In fact just 10% reported their fraud to the Charity Commission even though this is one way in which an organisation can help itself *and* help prevent the fraudster from moving on to exploit another charity.

The follow-up interviews underlined the potential value of third parties in helping to stop the fraud and in dealing with the aftermath. Most interviewees were satisfied with the response they received from the bodies they approached (these were primarily funders, the police and the Charity Commission).

**"...they [the charity] suddenly realised how vulnerable they were to fraud and how little money was left in the bank. And from that everybody seemed to pull together."**

Two-thirds of victims took action against their fraudster, mostly by referring the matter to the police (33%), by dismissing the individual (22%) and/or by launching civil recovery proceedings (13%). Half recovered some or all of the funds.

About a quarter took no action at all or didn't know what action had been taken. Some charities say they felt disempowered by bureaucratic obstacles. Others were frustrated at the time it took for their case to get to court – if it got there at all.

Almost half of all victims believe that they took all reasonable precautions to protect themselves (47%). Even so, two-thirds made changes to their procedures or enhanced their controls as a result of their fraud. The most commonly cited changes were to banking procedures (28%) or a general tightening of rules or procedures (22%). Several charities asked their audit committees or an external advisor to examine their procedures and to recommend improvements.

Charities that changed their procedures only after a fraud had been committed realise that they should have taken action sooner. They describe this as *"locking the stable door after the horse has bolted"*.

Just over half think that, in retrospect, they contributed to the fraud by, for example, being too trusting (31%) or by not having better risk management systems and procedures in place (23%).

## Concluding comments

Firstly, it's important to say that there is much to be reassured by here. Overall the incidence of fraud among charities appears to be much less than elsewhere in society, and when fraud does occur it tends to involve much smaller sums. Those who donate their time – the legions of volunteer workers – are not, after all, the sector's Achilles Heel, and nor are the country's many amateur fundraisers. In fact, the greatest threats exist where they are, arguably, easiest to tackle; among paid employees in the offices of the charities.

But this picture is by no means cause for complacency. The experiences of our charities suggest that in England and Wales thousands of them will fall victim to fraud each year. The biggest worry surely attaches to the smaller charities, of whom three-quarters have no anti-fraud measures in place. Of course the limited resources of these organisations are a big part of that story. But they are also the charities that can least afford the cash or reputational costs of even a small fraud. And remember, the vast majority of the 170,000 charities in England and Wales are small ones.

As economic times get harder, the dangers fraud poses will grow. Inertia is not an option. As this survey shows, the charitable sector as a whole has a pressing need for a much more rigorous engagement in tackling fraud – not just by the charities themselves, but by their professional advisors, law enforcers and regulators too. But it will also benefit from more clarity about where the real threats lie and who can help charities to defuse them.

**"It didn't occur to us at the beginning that this could possibly be criminal activity within our own ranks."**

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## Chantrey Vellacott DFK LLP

Chantrey Vellacott DFK is a long-established firm of Chartered Accountants, tracing its roots back over 200 years to 1788. The firm provides a broad range of professional services to an extensive client list covering the commercial, public and charity sectors.

Chantrey Vellacott DFK is a leading member of DFK International, a worldwide association of independent accounting firms and business advisors. This means the firm can readily provide clients with access to local expertise and information through the 300 DFK International offices worldwide.

Chantrey Vellacott DFK advises a substantial portfolio of over 300 clients in the not-for-profit sector and is ranked in the top 10 "Charity Finance" table of best auditors. With a strong Fraud & Forensic team the firm provides charities with counter-fraud solutions in terms of prevention, detection, asset tracing and the recovery of funds.

[www.cvdfk.com/fraud](http://www.cvdfk.com/fraud)

## The Fraud Advisory Panel

The Fraud Advisory Panel is a registered charity which works to raise awareness of the immense human, social and economic damage caused by fraud and to help individuals and organisations develop effective strategies to prevent it.

The Panel works to:

- advise government, business and the general public on fraud prevention, detection and reporting;
- assist in improving education and training in business, the professions, and the general public; and,
- establish a more accurate picture of the extent, causes and nature of fraud.

The Panel has a truly multi-disciplinary perspective on fraud. Members of the Panel include representatives from the law and accountancy professions, industry associations, financial institutions, government agencies, law enforcement, regulatory authorities and academia.

[www.fraudadvisorypanel.org](http://www.fraudadvisorypanel.org)

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