Myth: Audits Uncover Fraud

While independent audits serve an important purpose and may prevent potential fraud, audits rarely detect fraud. Even when an organization conducts an independent audit or review of its financial statements, the auditors do not guarantee that the organization is free from fraud. Independent audits only provide reasonable assurances that the financial statements are free of misrepresentations. To detect fraud, one would have to recognize the deception or misstatement of truth in the nonprofit’s financial statements. Because the auditor has to rely on the nonprofit’s representations about its own financial position, it is actually quite difficult for the independent auditor to detect fraud while conducting an audit. Instead, when you consider ways to reduce the risk of fraud at your nonprofit, think about governance, as explained in this article: Nonprofit Fraud: It's a People Problem so Combat it with Governance (Nonprofit Quarterly)

Did you know?

Audits are not the most effective way to uncover fraud: most frauds are discovered as a result of a tip, according to the Association of Certified Fraud Examiners’ (ACFE). Smaller organizations tend to experience disproportionately higher losses; but overall the majority of organizations studied each year use audits as ONE of several anti-fraud controls. ACFE recommends educating employees to detect fraud as key to preventing and detecting workplace fraud. A strategy to raise awareness
The role of internal controls
While an independent audit may not uncover fraud, strong internal controls can help reduce the risk of theft, fraud, and embezzlement. Internal controls sound daunting, but there are numerous very practical steps every nonprofit can take (even those with very few staff members) to put up barriers to theft and embezzlement in the nonprofit workplace. When auditors conduct an independent audit one of their "tests" is usually to determine the strength of a nonprofit's internal control, i.e., are policies in place, followed, and followed consistently? See our page on internal controls for more information and resources.

Additional Resources

- Are auditors responsible for detecting fraud? (CLA)
- I have a complaint (Nonprofit Risk Management Center)

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Disclaimer: The resources in this Guide are offered for informational purposes only. The National Council of Nonprofits recommends consulting a lawyer or accountant who has expertise in accounting rules for charitable nonprofits so that you can be confident that your charitable nonprofit is in compliance with all legal requirements. And, when your organization is looking for trusted information about financial management practices, good governance, and accountability, don’t overlook the resources that membership in your state association of nonprofits can provide.