Donors Want Board Action, Not a Lawsuit, When Fraud Occurs

By Alex Daniels

The Theory

When an employee embezzles money, taking that person to court isn't necessarily the best way to stay in the good graces of donors. A recent study led by John Lauck, an accounting professor at Louisiana Tech University, found that donors were more inclined to keep giving to a nonprofit if the board addresses the fraud.

The Test

Study participants were told to imagine they had given $250 to a nonprofit whose chief financial officer later was caught stealing. Lauck provided several scenarios: The organization prosecuted the CFO, fired the chief executive officer (who didn't know about the fraud until after it was exposed), issued a public apology, or reorganized the board by requiring directors to have financial expertise, stipulating that no employees can serve on the board, and ensuring regular reviews of the nonprofit's finances.

The Results

Neither taking the CFO to court nor sacking the CEO moved donors to maintain their previous level of donations. In fact, donors said they would give even less, on average, if the CEO had been fired than if the nonprofit had done nothing. But the board reorganization prompted donors to say they would give more than in the past.

Dig Deeper

In business, it is a commonly accepted principle that victims of fraud should restore their reputations by taking legal action against perpetrators, Lauck said. But nonprofits may fear the reputational hit from a lengthy public court fight. By not taking action, nonprofits may satisfy donors, but they risk letting fraudsters, who are often repeat offenders, go scot-free. "It would be best for the entire nonprofit community for them to be publicly criticized and perhaps prosecuted," he said.

Find It

"Fraud in the Nonprofit Sector: Rebuilding a Charitable Image," by John R. Lauck and John A. Brozovsky, was published in the *Journal of Accounting, Ethics and Public Policy,* Vol. 19, No. 2, 2018.