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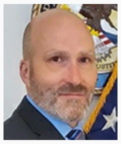

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Grant fraud in nonprofit organizations: Insider threat

By Jeffrey Ball

Great news! Your organization just received a large federal grant to provide counseling services to victims of domestic violence. This is welcome news for your organization, as it can now expand its services and hire additional staff. Now, the hard work begins: monitoring and oversight of the public funds entrusted to you. Is your organization ready to protect the public dollars it has been entrusted with to ensure they are used in accordance with grant rules and the law?

Every year, federal, state, private, and nonprofit groups award billions of dollars in grant funds to organizations of all sizes to deliver services, pay staff salaries, fund programs (e.g., scientific research, public housing assistance, food programs, refugee resettlement), and myriad other uses. Unlike a loan, grants need not be paid back; however, they do come with a significant number of rules and conditions that, if not followed, may cause your organization significant harm—including ineligibility to receive future grant funding and potentially criminal liability.

While many organizations hire grant writers and consultants to write proposals and complete grant applications, these same organizations often fail to have the proper infrastructure in place to ensure compliance with grant rules. This can be a confusing mixture of federal and state regulations, including obscure references to such documents as U.S. Office of Management and Budget circulars.

And if the rules and regulations are not enough to keep an organization on its toes, fraudsters also lurk around the corner, looking to take advantage of poor oversight. Ineligible individuals may seek to obtain services or funds from your organization through fraudulent means—such as misrepresenting their income level or number of dependents to receive benefits they are not entitled to. More likely, employees of your organization may commit fraud against a grant by billing for services that were not delivered, misusing the funds, or through self-enrichment schemes that could involve conflicts of interest.

Is all that enough to make your head spin? Let's take a closer look at some particulars to protect your organization from both mistakes and fraud.

Receiving and using grant funds

Many organizations seek grants and depend on them for a large portion of their funding. Grants can be a predictable and sustainable funding source for nonprofits and other organizations that can bridge the gap between donations and other economic variables. But, as mentioned, grants come with responsibilities. As a recipient of public funds—federal and state grants are publicly funded through tax dollars—your organization has become the steward of those funds.

You are obliged to ensure the funds are spent in accordance with the intended purpose for which you requested and received the grant. In most cases, you cannot use grant funds for a purpose other than which they were awarded. In other words, if the grant was to pay all or a portion of staff members' salaries, the organization cannot simply decide to buy new computers with the money instead. Some grants require organizations to submit proof of payment or purchase to draw down funds. Others allow organizations to draw down the funds to pay for allocated expenses and may not require specific documentation when the funds are disbursed; however, the organization must be prepared to demonstrate how the funds were used if requested. In virtually all circumstances, an organization must be prepared to account for and justify all expenses paid with grant funds.

Typically, state grants are largely funded through federal program dollars provided to the states in block grants. The states then provide funding opportunity announcements to notify organizations that funding for various purposes is available. Organizations then request funding under the criteria of each grant.

The funding announcements and grant applications usually contain all the rules for administering the grant if received. Typically, during the application process, organizations submit a budget detailing how the funds will be used, for example, to pay salaries, hire counseling services, conduct or attend training, purchase equipment, and other related costs. It is important to note and be familiar with the specific federal and state regulations cited as the controlling statutes in the application to ensure your organization knows what types of expenses are allowed. For example, applications for U.S. Department of Justice (DOJ) grants will reference the most recent version of the DOJ Financial Guide as well as Title 2 U.S. Code of Federal Regulations (C.F.R.) Part 200, Grants and Agreements, that provides uniform administrative rules for grants across the federal government.[1] Additionally, each grant and each agency will likely have rules and conditions specific to that grant. The final grant agreement or contract will likely incorporate the rules from the application by reference. As an aside, states often award grant funds in the form of a contract to an organization, and the receiving organization may award subcontracts to contractors for services (for example, counseling services). However, DOJ, for example, still views organizations that receive grants and provide subawards as grant recipients or subrecipients, not contractors.

While it is not a requirement under DOJ grants to have a separate financial account for grant funds, the organization must be able to trace the receipt and use of these dollars through its financial and accounting system. This is particularly important if the organization receives multiple grants that are used to fund portions of employees' salaries or are divided across multiple projects and/or commingled with other nongrant funds in a single account.[2]

It is also essential to know what types of expenses are prohibited under most grants. For DOJ grants, funds cannot be used to pay rent or a lease if the lease is being paid to one of the principals (recipients) of the organization, such as a board member or executive director. For example, if an organization rents its office space from a board or staff member, grant funds cannot be used to pay this rent due to the obvious potential for abuse and conflict of interest.[3]

It should go without saying, but grant funds cannot be used for personal enrichment. However, that does not stop individuals from misusing grant funds to pay for personal expenses or specifically prohibited items such as alcohol or entertainment activities.