

# *Goals for 2010 & beyond*

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2010 PLA CONFERENCE - SPIER - WESTERN CAPE  
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- Speaker* Steven Powell
- Company* Edward Nathan Sonnenbergs
- Topic* Early detection of fraud and scams – warning signs for trustees

# objectives?

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- to create awareness of the impact of the negative economic climate on the fraud risk
- theory regarding fraud in general
- The general fraud threat versus
- pension fund fraud threats
- EFT abuse
- fraud prevention and internal controls
- case studies

# the impact of the recession on staff

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staff are financially distressed

spiralling debt and the inability to manage debts is a massive factor inducing fraud and corruption

micro lending impact

importance of monitoring the situation in key finance positions

the risk for pension funds arises from fund managers under pressure

controls must be tighter than ever

# understanding the fraud risk

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The fraudster in any organization is your most capable, most reliable, most trusted employee - mr fixit!

more than 80% of all frauds involve employees, most of whom have more than 5 years of service

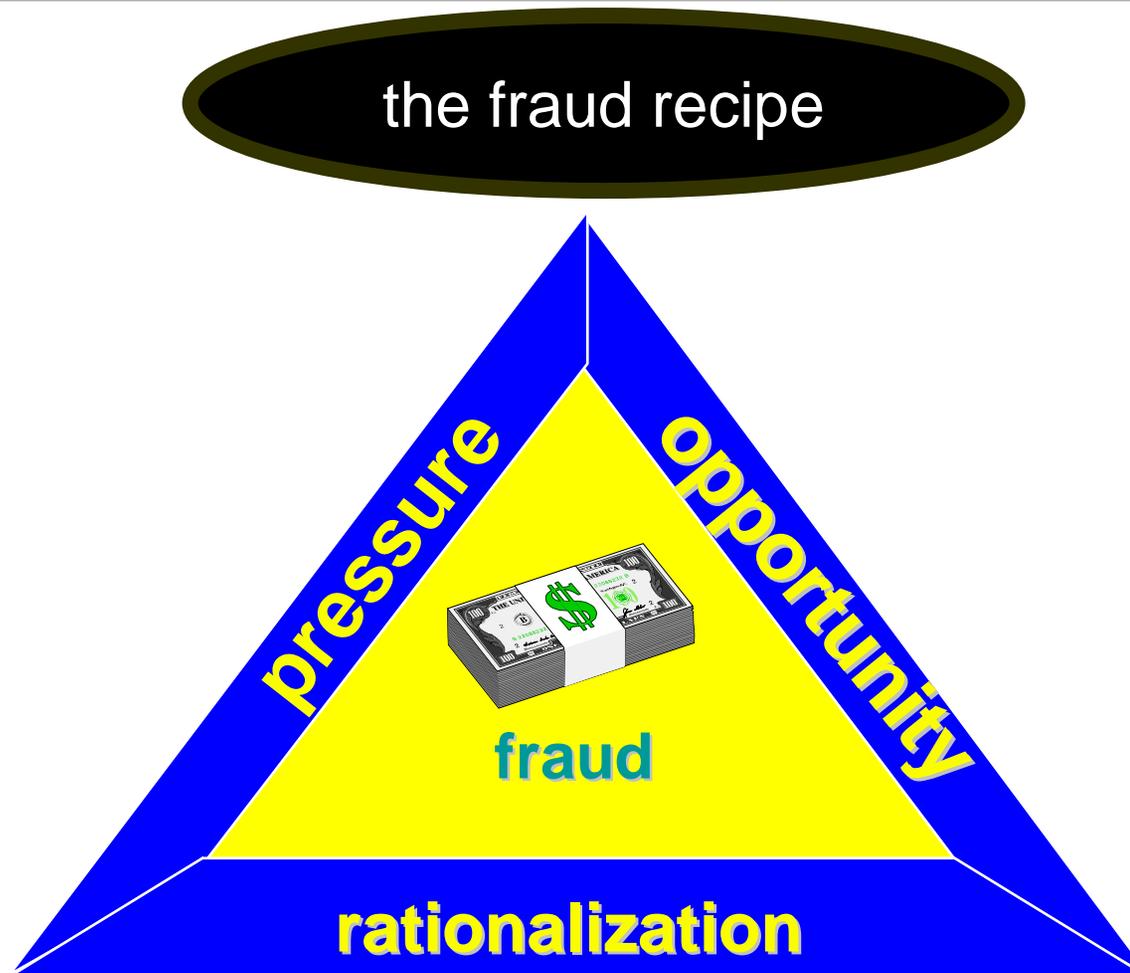
## TRUST REPLACES THE CONTROLS

generally:

- older than 30, higher percentage are male, stable family situation, above average education, first offender

# the fraud triad - *Psychology behind fraudulent conduct*

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# fraud pressures

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- living beyond means
- insecurity regarding tenure of position
- trigger events
  - divorce
  - extra marital affairs
  - medical emergency
- peer pressure
- gambling alcohol or drug problems

# opportunity

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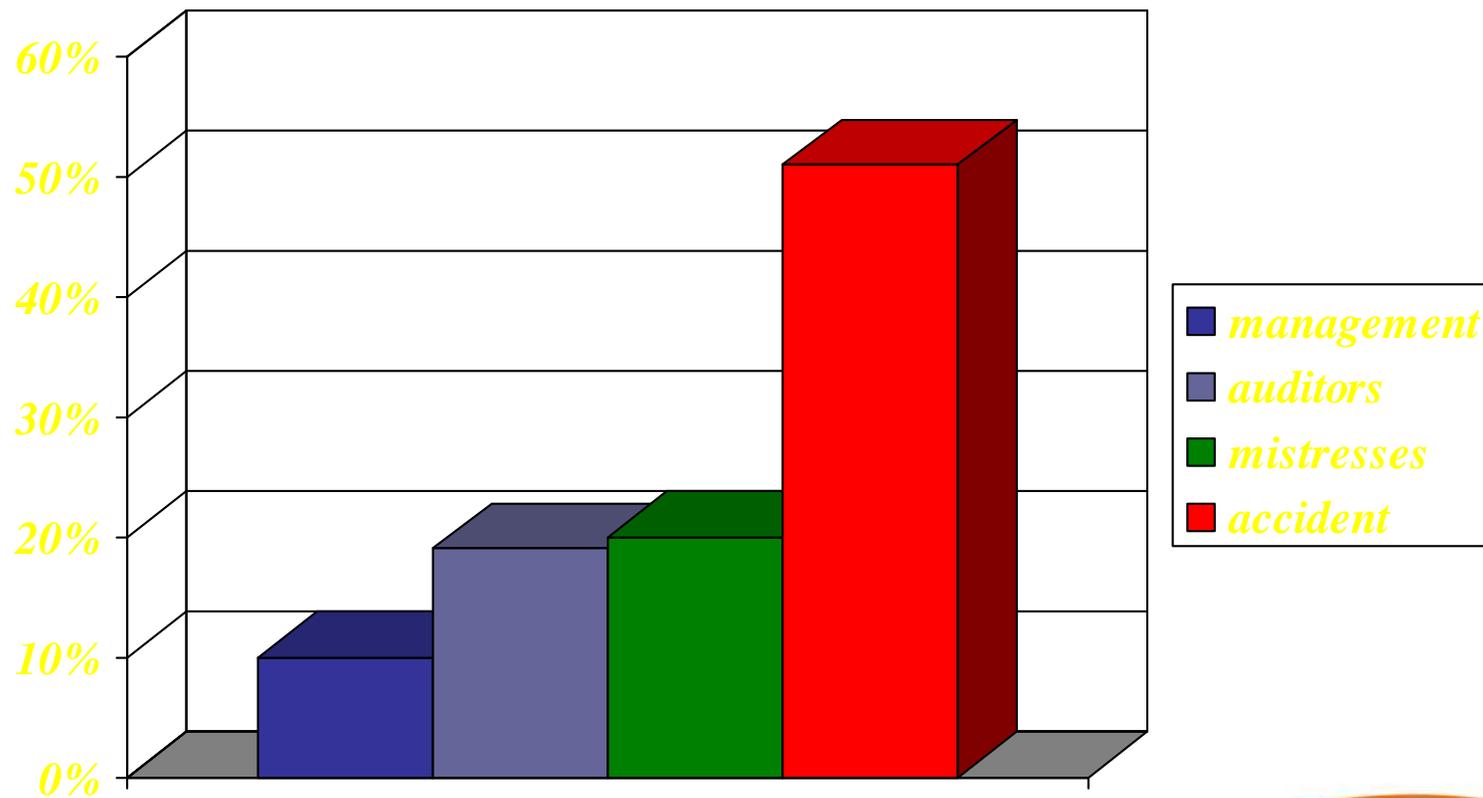
- poor control environment
- remote location
- shared passwords
- limited segregation of duties
- limited independent review
- high trust

## examples of “rationalizations”

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- “it was just a loan I am going to pay it back”
- “it was a spotters fee”
- “it was just a commission”
- “the company does not pay enough money for us to survive”
- “the company has retrenched a lot of staff”
- “i should have been promoted long ago”

## detection of fraud



# EFT fraud definition

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EFT fraud is essentially the diversion of funds from the organisation's bank accounts to third parties, to whom those funds are not due, usually involving manipulation of the vendor payment system

# key controls

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- vet vendors properly (address, history, bank account, expertise & infrastructure)
- enforce tight control over changes to suppliers bank accounts – add management authorisation
- audit changes to supplier banking info over the past year
- interrogate the changes
- verify with suppliers and banking institution

# Pension fund frauds

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**Pension fund fraud** happens when unscrupulous fund managers purposely misappropriate funds for personal gains

**Pension fund corruption** happens when personal or political interest takes precedence over the interests of the fund

NEW YORK—A former top investment officer for New York’s state pension fund admitted Wednesday that he helped channel hundreds of millions of dollars in public retirement money to investment firms that paid kickbacks to officials to get the business.

David Loglisci pleaded guilty Wednesday to a securities fraud charge, becoming the highest-ranking member of former State Comptroller Alan Hevesi’s administration to admit a role in the “pay-to-play” scheme.

“Investment decisions were made in part according to political benefit for the comptroller, rather than exclusively in the best interests of the people,” Loglisci, 38, said in a statement read in court. “The political motivations for investment selection were chronic and institutionalized throughout the office, creating a culture of corruption at the highest levels.”

(\$150 billion fund) Associated Press 11 March 2010

SA – Fidentia – SETA pension funds invested - allegedly in exchange for kickbacks

# Madoff, Tanebaum, etc

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If the returns sound too good to be true – they probably are - steer clear  
Beware of the Ponzi scheme

## Investment fraud:

- Inside information almost always means fraudulent information by paid promoters.
- There is no way you can turn R100 into R100 000 in six weeks -this is a pyramid scheme
- There is no such thing as risk free investing, guaranteed returns, or spectacular profits

there are always takers for fraudulent schemes

# Preventing pension fund fraud

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**Fraud can happen at any institution but when big money is involved, it is imperative that fiduciaries and stakeholders take the necessary measures to prevent fraud from occurring in the first place. Key checks include:**

- Rigorous background checks/lifestyle audits on fund managers
- Strong conflict of interest policy, coupled to,
- Annual declaration of interests
- Strong gift policy – no free trips or valuable gifts for trustees
- Anonymous tip-off facility in place with strong protection for whistleblowers
- Ensure that investment, operational and risk management due diligence is performed prior to recommending an investment
- Detect and act on early warning symptoms
- Get independent forensic experts to perform annual fraud risk assessments
- Avoid gaining comfort from other blue chips that have also invested
- Scrutinize the annual financial statements and act quickly when these are delayed
- Look at prevailing market conditions, - be sceptical of incredibly high returns

# Entertainment versus corruption

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Many in the investment community consider “travel and entertainment” for pension fund clients to be normal marketing; the kind of thing that “everybody does” because if they don’t their competitors will. This is how business is conducted in the marketplace. Some investment firm representatives say that their firms get upset if they don’t spend their marketing budgets to get “face time” with clients.

Depending on the amounts of money involved, this can easily cross over into corrupt activity in terms of the Prevention and Combating of Corrupt Activities Act. (Act 12 of 2004)

# new definition of corruption

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under the new act, any person who directly or indirectly gives or accepts or agrees or offers to give or accept any gratification from another person with the purpose of acting personally or influencing another person to act in a manner that amounts to an illegal, dishonest, or unauthorized action or an abuse of authority, a breach of trust, or a violation of a legal duty, is guilty of an act of corruption

## “gratification”

the term “gratification” has purposefully been very widely defined. it incorporates money, donations, indemnities, offers of employment, discharge of a debt, the granting of favours, rights or privileges, aid, votes, consent or benefits of any kind.

## Duty to report corruption (ito section 34 of Act 12 of 2004)

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Any person in a position of authority who knows, ought reasonably to have known or suspected, that an act of corruption, fraud, theft, extortion, forgery or uttering has been committed, that person is obliged to report the matter to the SA Police Services.

Non reporting is a criminal offence where the value involved exceeds R100, 000.00

# Lifestyle audits

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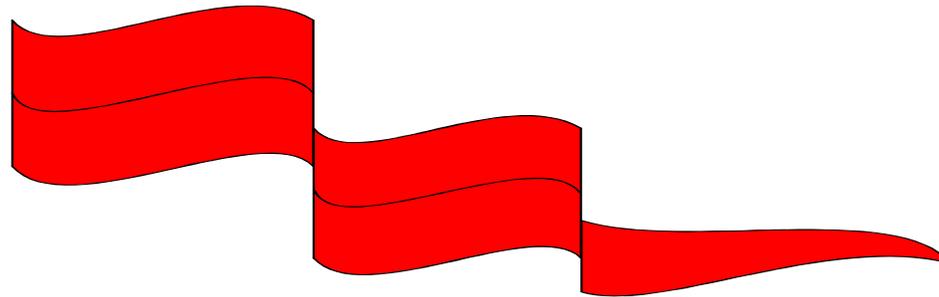
- Properties
- Vehicles
- Credit
- Companies

There are a variety of public databases that can be accessed to determine if the lifestyle is commensurate to income stream and further to detect potential conflicts of interest as well as whether or not individuals are under financial pressure and may be susceptible to fraud or corruption

the symptoms of fraudulent behavior

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the fraud red flags or warning signals are  
always present - make sure that staff know  
what to look out for



# Individual fraud red flags

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- excessive lifestyle
- gambling alcohol or drug problems
- staff who constantly claim underpaid
- close relationships with suppliers
- poor credit rating
- poor communication and reports
- indulging in affairs
- not taking leave
- refusal of promotion
- excessive & unexplained overtime
- criminal record

## divisional red flags

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- too much trust placed in key employees
- limited segregation of duty
- no independent checks on reconciliation and payments
- no clear lines of authority or responsibility
- proper authorization procedures not enforced
- inadequate documentation & records
- infrequent independent reviews
- inadequate disclosure of interests & investments
- management override of the controls
- operating on a crisis basis
- inadequate attention to detail

# conclusion

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be prepared, prevention is better than cure

promote a strong ethics culture

put stringent controls in place, including conflict of interest, declaration and gift policies as well as whistleblower protection – test for compliance

perform lifestyle audits on key players

perform rigorous due diligence on large investments

get independent forensic specialists to perform an annual fraud risk assessment

perform control review regarding eft payments

do not rely only on controls - only as effective as the people enforcing

train people to recognize the symptoms

do not work in a vacuum - use the tools and technology & experts

*Thank you*

QUESTIONS ARE WELCOME

**PENSION LAWYERS**  
ASSOCIATION

*Goals for 2010 & beyond*

thank you

tel +2721 410 2553

cell 082 820 1036

[spowell@ens.co.za](mailto:spowell@ens.co.za)

[www.ens.co.za](http://www.ens.co.za)

