



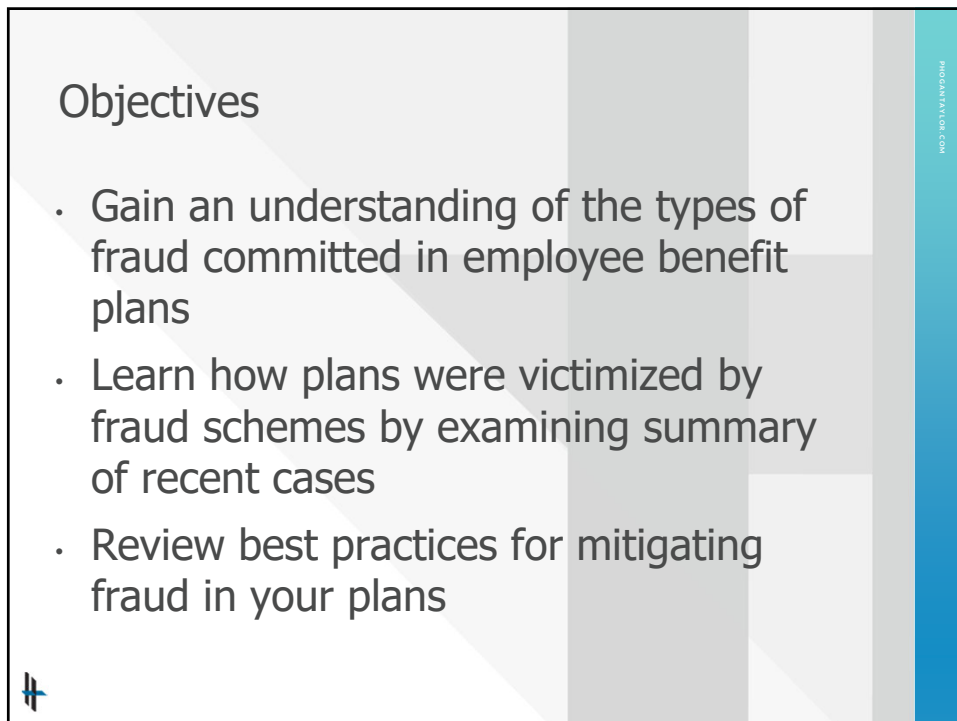
Keeping Hands Out  
of the Cookie Jar!

Fraud in Retirement Plans

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1



Objectives

- Gain an understanding of the types of fraud committed in employee benefit plans
- Learn how plans were victimized by fraud schemes by examining summary of recent cases
- Review best practices for mitigating fraud in your plans

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2

## Types of Fraud

- Fraud committed against a plan
  - Misappropriation of assets
- Fraud committed by a plan
  - Financial statement fraud

3

## Common Misconception

“There is no fraud in my plan because I received a clean audit.”

4

## Plan Audits – Do NOT

- Guarantee fraud or errors will not occur
- Guarantee management/staff will abide by controls
- Guarantee fraud or errors will be detected
- Guarantee collusion will not occur



5

## The Fraud Triangle

- Opportunity
- Incentives/Pressure/Motivation
- Rationalization/Justification



6



## Who Commits the Fraud?

Outside the Plan

- Custodian
- Trustee
- TPA
- Recordkeeper
- Investment advisor
- Hacker/identify theft

Inside the Plan



- Plan administrator
- Participants
- HR/Accounting/Plan management



7

## Vulnerability to Fraud

- Conflicts of interest
- Lack of...
  - Attention
  - Expertise
  - Oversight



8

## Warning Signs and Red Flags

- Excessive or unusual turnover
- Social media/hotline calls
- Inconsistent timeliness of contributions
- Frequent changes in consultants
- Plan sponsor financial difficulty
- Ceasing of contributions
- Excessive distributions



9

## Common Fraud Schemes

- Theft and embezzlement of plan assets using wire transfers, forged checks and other means
- Failure to deposit employee contributions into the plan
- Funneling contributions into a secret account or perpetrator's account
- Unauthorized withdrawals
- Unauthorized use of plan assets to invest in other business interests
- Defrauding the company by issuing duplicate paychecks
- Kickbacks
- Identify theft/cyber theft



10

## Common Fraud Schemes – H&W

- Embezzling health care premiums from payroll withholdings
- Misappropriating client-provided funds from the company's claims account
- Failing to pay health claims
- Defrauding insurance companies by submitting fraudulent insurance claims and doctor's notes to insurance companies
- Paying claims to fictitious individuals for services that were never rendered
- Submitting false claims for reimbursement of prescription drugs
- Premium overpayment/unauthorized



11

## ERISA Civil Violations

- Failing to operate the plan prudently and for the exclusive benefit of participants;
- Using plan assets to benefit certain related parties to the plan, including the plan administrator, plan sponsor, and parties related to these individuals;
- Failing to properly value plan assets at their current fair market value or to hold plan assets in trust;
- Failing to follow the terms of the plan
- Failing to properly select and monitor service providers
- Taking any adverse action against an individual for exercise his/her rights under the plan



12

## How Is Fraud Discovered?

- Whistleblower
- Tips from plan sponsor employees, participants, beneficiaries, third-party administrators
- Review of Form 5500
- Referrals from law enforcement  
DOJ, FBI, SEC, FINRA

13

## Employee Benefits Security Administration (EBSA)

EBSA oversees approximately 747,000 retirement plans, 2.5 million health plans, and 673,000 other welfare benefit plans.

These plans cover 152 million workers, retirees, and dependents

The retirement plans alone hold an estimated \$12 trillion in assets

14

## EBSA 2022 Outcomes

- Recovered **\$1.4 billion**
- Closed 907 civil investigations with 585 cases (66%) resulting in monetary results for plans or other corrective actions.
- Closed 164 criminal investigations which led to the indictment of 86 individuals



15

## Consideration of Fraud in a Financial Statement Audit

- The distinguishing factor between fraud and error - **intentional** versus unintentional
- The auditor is primarily concerned with a **material misstatement**
- The primary responsibility for the prevention and detection of fraud rests with **those charged with governance** of the entity and **management**
- An auditor is responsible for obtaining reasonable assurance that the financial statements as a whole are free from material misstatement, **whether caused by fraud or error**



16



## Fraud Risk Factors – Misappropriation of Assets

Incentive/Pressure	Opportunity	Attitude
Known financial pressures for key plan employee	Lack of oversight	Changes in behavior or lifestyle
Employee dissatisfaction – more work, same pay	Limited segregation of duties	Disregard for internal controls
Promotions or other rewards inconsistent with expectations	Inadequate management understanding	Failure to correct deficiencies



17

## Fraud Risk Factors – Financial Reporting

Incentive/Pressure	Opportunity	Attitude
Financial or other instability of sponsor	Management = governance	Tone at the top
Poor investment results	Significant estimates	A disregard for regulatory environment
Underfunded position	Lack of oversight	Overreliance on third parties
New requirements – accounting or regulatory	High turnover rates	Lack of transparency



18

## Examples of Fraud

AICPA Employee Benefit Plan Audit Quality Center

Publication - ***EBP Fraud Examples***

Grouped by significant area

Distributions

Expenses/forfeitures

Participant loans

Eligibility

Contributions

Investments



19

## Case Study #1

NY: A business owner, controller, and payroll administrator of Navillus Construction Company devised a fraudulent scheme to avoid making required contributions to health, pension and vacation benefit plans required by union contracts

Up to 20 years in prison for each; restitution pending



20

## Case Study #1

**Perpetrator** – Donal O’Sullivan, Padraig Naughton, and Helen O’Sullivan

**Victim** – Workers entitled to benefits for “covered work”

**Scheme** – Placed certain workers on the payroll of another company (consulting company) to avoid making contributions to plans for those workers. To avoid detection created fraudulent invoices for “consulting” to reimburse the consulting company for workers pay



21

## Case Study #2

**NJ:** An administrator  
embezzled \$140K

6 months confinement, three  
years probation



22

## Case Study #2

**Perpetrator** – George Laufenberg

**Opportunity** – Lack of proper segregation of duties – had authority and operating control

**Motive** – Greed/personal gain

**Scheme** – Deferred compensation payments to which he was not entitled



23

## Case Study #3

Kansas City, MO: A business owner embezzled \$31K in contributions from a defined contribution plan and \$4.3 million in fraudulent loans from a bank and identity theft.

50 months in prison, 5 years supervised release; \$4.3M in restitution.



24

## Case Study #3

**Perpetrator** – Brenda Wood

**Victims** – Plan, participants, and a bank

**Opportunity** – Lack of proper seg of duties – had authority and operating control

**Motive** – Greed/Personal gain

**Scheme** – Did not remit EE deferrals to the plan but kept them for personal use and took fraudulent loans

**Detection** – Participant complaints of missing funds

**Prevention** – Proper segregation of duties and reconciliation of funds withheld to that remitted to the Plan



25

## Case Study #4

EBP manager embezzled > \$420K from a university pension plan by making unauthorized changes without proper approval to participant data (changed bank account info and mailing addresses) for six former employees (one retired and 5 deceased)

Prison, three years supervised release and restitution.



26

## Case Study #4

**Perpetrator** – Crystal Duncan Baker

**Victim** – Plan and participants

**Opportunity** – Poor internal controls. Access to make changes with no monitoring controls

**Motive** - Personal gain – used money for personal expenses and benefit

**Scheme** - Changed bank account, routing info and mailing address to her own

**Prevention** - Proper segregation of duties – review of change report (monitoring control) and better internal controls



27

## Case Study #5

Fort Smith, AR man received investment funds over a 5 year period from 25 different clients which were not invested but used for personal use (renovated home, paid personal expenses, took vacations, made cc pmts, and *contributed to local charities*), to pay back other investors and embezzled from a EBP

Sentenced to 150 months in prison, restitution of \$5.7M to victims



28

## Case Study #5

**Perpetrator** – William Jackson Moates, Jr.

**Victim** – Investment clients and EBP participants

**Opportunity** - Signing authority to link accounts and transfer money, redirected funds, improper administration of EBP; he never set up the EBP plan in the Plan Sponsors' names but his own, improper distribution requests from annuities

**Motive** - Greed, personal gain

**Scheme** - Fabricated documents (Ponzi scheme)

**Prevention** - Authentication of statements; confirmation with custodian directly



29

## Case Study #6

Dallas TPA who performed benefits administration embezzled \$14 million of plan assets for personal and business use by requesting unauthorized distributions from clients EBPs' trustee/custodian and provided false reporting statements to the plans to cover up the scheme.



30

## Case Study #6

**Perpetrator** – TPA and Recordkeeper

**Victim** – Plans, plan fiduciaries and participants

**Opportunity** – Lack of monitoring service providers

**Motive** - Greed, personal use and business expenses

**Scheme** – Misappropriation of assets; unauthorized distributions; fabricated plan and participant statements, excess fees

**Detection** – Whistle blower led to Oct 31 raid by FBI

**Prevention** – Better controls, direct receipt and communication with custodian, reconcile sum of participant statements to custodial statements



31

## Other Examples of Fraud

- A hacker used personal information of a participant to gain access to his Plan account and withdraw \$60,000 as a hardship distribution; another hacker took a \$13,000 loan in which the participant is making loan repayments through payroll deductions
- The son of a deceased beneficiary received benefit payments from August 2011 through February 2018 totaling \$39,829, which was intended for his mother who died on July 29, 2011
- A participant's wife submitted fraudulent pharmacy receipts to Health and Welfare Plan for reimbursement, which were altered to appear as though they were written for members of her family
- An Employer failed to remit \$210,915 in health premiums deducted from employee's salaries. Although these funds were deducted from employee's salaries, the employer failed to remit them to the insurer. As a result, the insurance company terminated the health coverage retroactively, resulting in unpaid medical claims



32



## Basics Steps to Mitigate Risk of Fraud

### Implement internal controls to monitor your exposure to fraud:

1. Review and reconcile reports provided by the record keeper and the custodian for plans with participant account balances
2. Spot check and recalculate payroll
3. Review and recalculate distributions and vesting calculations for selected benefit payments
4. Review and understand expenses paid by the plan to service providers
5. Monitor access rights to payroll and recordkeeping

33

## Example Controls to Mitigate Fraud

### Participant data:

- Employee participation refusals ('opt-outs') are retained for future reference.
- Maintenance of participant data is segregated from responsibility for benefit approval or processing.
- All participant-initiated enrollments, transfers, changes in investment allocations, and other change requests must be authorized by the participant.
  - The ability to perform these activities electronically or directly with a third-party administrator is restricted to authorized participants through the use of specific identification and a personal identification number. Invalid attempts to access and perform functions are reviewed and investigated.

34

## Example Controls to Mitigate Fraud

### Contributions:

- Cash is independently controlled upon receipt.
- Procedures are in place to monitor that cash receipts are deposited intact daily.
- To prevent theft, checks are restrictively endorsed upon receipt.
- Procedures are in place for the segregation of duties between the responsibility for receiving contributions and for the processing of contributions.
- Bank and investment accounts are reconciled monthly.
- Remittance Policy
  - Past-due contributions are investigated on a timely basis.
- Secure access to computerized contribution records is limited to those with a logical need for such access

35

## Example Controls to Mitigate Fraud

### Investments:

- Responsibility for investment decisions and transactions is segregated from the custodian's functions.
- Financial stability of financial institutions holding investments is reviewed.
- Written-off investments are reviewed for possible appreciation.
- Documents are controlled in a limited-access, fireproof area.
- Securities held by custodians are confirmed.
- Secure access to computerized investment records is limited to those with a logical need for such access.

36

## Example Controls to Mitigate Fraud

### Benefit payments:

- Responsibilities for benefit approval, recording of benefits, and maintenance of participant files are adequately segregated.
- Periodic correspondence with retired beneficiaries is maintained, and correspondence or payments are returnable to plan committee if undeliverable.
- Check endorsements are compared with signature in applicable participant records.
- Supporting documents are effectively canceled on payment.
- Secure access to computerized benefit payment records is limited to those with a logical need for such access.



37

## Internal Controls

Custody vs Authorization - No one person should –

- Initiate transaction
- Authorize transaction
- Record transaction
- Reconcile balances
- Handle assets
- Review reports



38

## Other Considerations

- Training/cross training
- Mandatory vacations
- Exception reports
- Claims audits
- Death audits
- Password rotation
- Review of cancelled checks
- Monitoring and/or engaging a third party service provider to review plan transactions



39

## DOL's Ten Warnings Signs That Your 401(k) Contributions Are Being Misused




- Your 401(k) or individual account statement is consistently late or comes at irregular intervals – or not at all!
- Your account balance does not appear to be accurate
- Your employer failed to transmit your contribution to the plan on a timely basis
- There was a significant drop in your account balance that cannot be explained by normal market ups and downs
- 401(k) or individual account statement shows your contribution from your paycheck was not made




40

## DOL's Ten Warnings Signs That Your 401(k) Contributions Are Being Misused



- Investments listed on your statement are not what you authorized
- Former employees are having trouble getting their benefits paid on time or in the correct amounts
- Unusual transactions, such as a loan to the employer, a corporate officer, or one of the plan trustees
- Frequent and unexplained changes in investment managers or consultants
- Your employer has recently experienced severe financial difficulty



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41

# Questions?

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42