

# FINANCIAL SERVICES COMMISSION

## 1<sup>st</sup> General Meeting of Members and Pensioners of the RADA Pension Plan

Ascot Hall  
Old Harbour, St Catherine

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### **Your Pension in a Dangerous World**

Madam Chairman, trustees, parish managers, zonal directors, members, pensioners, ladies and gentlemen, good morning.

I have been receiving and reading with interest your newsletter "Coverage" put out by the trustees of your pension plan. These newsletters contain a considerable amount of information and advice in a digestible and reader-friendly form. This is an excellent initiative and establishes clearly that your trustees have taken to heart the objectives of the new regulatory regime. Indeed, they have gone beyond legal requirements in seeking to keep members and pensioners informed, a key theme in the new regulatory regime. Having read them, it is hard to know what else to tell you. Instead, I thought that it might be useful to place the law in context. To do so I propose to tell you a story.

## THE STORY

My story begins with a man by the name of Bennett. His name is not disguised for the purpose of this story. Patrick Bennett offered tax free investments. He said he would rent photocopier machines to various entities, including local government. This business was so lucrative that he could offer a very high return on the initial investment. Of course, in the early days the returns were paid. People got their interest as advertised by Mr Bennett. There was one lady, mature in years, whose husband had died. She was persuaded to invest the funeral grant she received from her insurance company. She was not alone; Mr Bennett targeted a lot of people like this lady. But even law firms invested in Mr Bennett's operation using some of their pension money. Yes, I will repeat that; even law firms invested using some of their pension money. Still, the majority of his investors were in the US\$5,000-US\$10,000 range. Because his operation was a Ponzi scheme he eventually found it harder to find new investors in this range. The immediate result was that he began to fall back on his promise to deliver the returns initially promised.

Meanwhile, Mr Bennett was living the high life. He was investing money in real estate including hotel properties, with one small wrinkle: he never made these investments in the company's name or in his own name. These investments were always made in his wife's name, or his father's name, or even in his children's name. Of course, his children went to the best schools, and life was good to him, you could say. It was all being funded by his little project - the Ponzi scheme.

One day, the United States Securities and Exchange Commission ("SEC"), for this story is a true story and it took place in America, went in and examined his

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books. They found that he should have been registered with the SEC. His investment arrangements with his investors were securities that should have been registered as well. They also found that he had misrepresented to investors that their return from the investment was tax free because their funds were being used to rent photocopier machines to municipalities, including New York City. It turned out that New York City never rented photocopier machines; it owned all of its photocopier machines. The investments that he was selling were based on a big lie.

The United States government moved in and prosecuted. Firstly, they asked the court for a temporary restraining order, which is an injunction that would effectively freeze everything as is. Mr Bennett's company employed some smart lawyers, however, who lost no time in filing for bankruptcy. The effect of that action was that the trustee in bankruptcy now had a job to do to gather up the assets of the company. It would not surprise you to learn that he had a great deal of difficulty in trying to find these assets and that the process involved lengthy drawn out litigation to find and get at them because the assets, for example, a hotel, would be in the name of, for example, Mr Bennett's wife. You see, from the perspective of the regulator, prosecutions may be brought, and they may even end in convictions and due punishment being meted out to the perpetrators of frauds such as this one. But, from the perspective of the investor who has lost money, fines and prison terms give them no money back and very little satisfaction. In the Bennett case, by the time the litigation was finished, there were only pennies on the dollar left. You can appreciate the pain and hopelessness that was their lot, particularly of the older people (many of whom were in their 60's) and pensioners who were left with virtually nothing and neither the time nor the means to rebuild or reacquire a nest egg.

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From time to time in the financial pages of the newspapers in Jamaica or on the talk shows or the verandas, you hear talk about “Ponzi” schemes, or pyramid schemes. Perhaps you have wondered what it means. You probably have some idea that these schemes involve something unsavoury or unseemly, something to be avoided. But you probably don’t trouble yourself too much about them. After all, most of us do not believe that we would be taken unawares by a Ponzi scheme. Most of us believe that the people who suffer when a Ponzi scheme collapses, as they all eventually do, are “other” people, that undefined collection of fools and unfortunates that we all profess to know but seldom can identify until after the fact, after the collapse.

So, what is a Ponzi scheme? Where better to learn about this than from the country where these schemes are spawned at an almost regular rate year in and year out, almost as if some attribute of human nature requires that they should exist? The following extract from the SEC’s website<sup>1</sup> explains.

*“Ponzi” Schemes*

*Ponzi schemes are a type of illegal pyramid scheme named for Charles Ponzi, who duped thousands of New England residents into investing in a postage stamp speculation scheme back in the 1920s. Ponzi thought he could take advantage of differences between US and foreign currencies used to buy and sell international mail coupons. Ponzi told investors that he could provide a 40% return in just 90 days compared with 5% for bank savings accounts. Ponzi was deluged with funds from investors, taking in US\$1 million during one three-hour period – and this was 1921! Though a few early investors were paid off to make the scheme*

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<sup>1</sup> <http://www.sec.gov/answers/ponzi.htm>

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*look legitimate, an investigation found that Ponzi had only purchased about US\$30 worth of the international mail coupons.*

*Decades later, the Ponzi scheme continues to work on the "rob-Peter-to-pay-Paul" principle, as money from new investors is used to pay off earlier investors until the whole scheme collapses.'*

In another case, hundreds of investors in the province of British Columbia in Canada were ruined by persons professing to be "servants of God". They trusted a devout man who promised them riches from a bank on a tropical island. Of course, he disappeared and so did their money. At first, payments from the tropical island arrived as promised, delivering returns as rich as 37 per cent. But the bank, which was in Grenada, by the way, was run like a Ponzi scheme. It used money from new investors to pay returns to earlier investors. It was backed with falsified assets and a sham insurer. Like many scams of its type, it sucked in naïve investors with the promise of astronomical returns from pitchmen professing to be servants of God. The bank collapsed in 1999 after duping investors of US\$200 million<sup>2</sup>. This was not small change.

## REGULATION

These stories are just a tiny sample from the financial literature. I wanted to tell you these stories because it is important to realise that this type of thing is going on somewhere in the world right now today. It is important to realise that if the persons operating these schemes are not already doing so today they will certainly be there trying to suck you in tomorrow. It is important to realise that you are no less vulnerable to falling prey to operators like Mr Bennett or the

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<sup>2</sup> <http://www.kycnews.com/Press/2001/01-x16.htm>

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“servants of God” than were their actual victims. Avoiding these dangers requires some diligence and a dose of common sense. If it seems too good to be true, you can be sure that it is too good to be true.

Governments around the world, and Jamaica’s has been no exception, have long recognised the danger that these predators represent to the financial safety and livelihoods of their citizens and have put in place laws and created regulators, like the Financial Services Commission (“FSC”), to help to keep their societies safe from financial predators. In Jamaica we have strong regulatory regimes to cover banking, insurance and securities markets. The FSC exercises vigilance and pursues every case that comes to its attention. But so does America have these laws and the SEC is almost a byword for extreme vigilance and vigour; and yet the Bennett case took place in America just 10 years ago. The reality is that governments and laws and regulators cannot protect investors from themselves. But when it comes to your pension, we can go a little further; and, indeed, it is well worth it to go a little further. This further step can make a world of difference to our lives and the lives of our families and communities. Of course, I am talking about the new pension regulatory regime. But I really want to emphasise just two crucial aspects of it.

## INVESTMENTS

The Investment Regulations create a legal framework of requirements governing the investment of pension funds. They set out the standards for sound pension fund investment practice. At the core of the Investment Regulations is the Statement of Investment Policies and Principles (“SIPP”) which documents how a fund’s investments will be managed. The SIPP must be produced by the trustees of each pension plan and reviewed by them at least once a year. It must

contain an outline of the plan's investment portfolio and related activities including its target assets and liabilities, risk assessments, liquidity and projected continuity, which should all be consistent with the plan's economic environment. During the year, the SIPP provides guidance to the trustees and their investment managers as to the types of assets into which the fund's monies can be placed and also the limits imposed on these investments. The SIPP framework provides a structured and systematic way to invest. Properly used, it gives to each pension fund the confidence that it is approaching the challenging task of investing prudently and profitably in a rigorous and safe manner that has been tried and tested the world over. This will result in better stewardship by the trustees and investment managers and reduced scope for the misuse of pension funds.

## GOVERNANCE

The Governance Regulations provide the broad framework for the management of pension funds. They set out the duties and responsibilities of trustees and make provisions for the promotion of good governance within pension plans. Their aim is to encourage the efficient use of resources and, equally, to require accountability for the stewardship of those resources. This responsibility is placed on the trustees of a pension plan but you, the members, also play a vital role.

The legislation provides for diversification of the members of the board of trustees in order to reduce the effects of possible conflicts of interest. So, for example, not more than 50% plus 1 of the trustees can be sponsor trustees. The rest must be nominated by the members and, in some cases, the pensioners.

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The trustees must meet at least once a year. You would be surprised to learn that in some pension plans the trustees do not meet every year. It is clear in the case of your pension plan that your trustees go well beyond this minimal legal requirement and, indeed, the FSC encourages trustees to meet as frequently as is necessary to properly oversee the pension plan.

Trustee meetings are needed not only to establish and review periodically the SIPP that I mentioned earlier but also to review regularly the performance of the plan's appointed agents and advisors, thus satisfying themselves of their continued suitability, that investment performance is meeting expectations and that the managers are investing funds in accordance with the SIPP. The trustees will also meet to establish written policies and procedures governing complaints procedures and conflict of interest procedures. They will meet to approve the annual report for members and to ensure that members are being kept fully informed in accordance with their rights under the legislation (annual benefit statements, members' handbook). An informed member is a member who is thereby empowered to take responsibility for his or her own financial future. An informed member is able to hold trustees and investment managers accountable for their stewardship. An informed member is able to assert and maintain his or her rights and thereby secure his or her financial future. In short, an informed member is able to participate.

Let us now recall the law firm that put its pension money in the Bennett funding scheme. How on earth could they do something like that? Undoubtedly, they had no SIPP; undoubtedly they did not have to disclose the details of what they were doing with the member's money; undoubtedly they did not choose to get or to follow professional advice; undoubtedly they were either greedy, foolish or negligent; undoubtedly they failed to follow a structured and systematic

approach to investing believing, perhaps, that through their brilliant insights they had discovered another genius who had in his possession the golden goose, or at least knew where to find it and steal its eggs; undoubtedly they abused their fiduciary duties and let down the trust that was placed in them. The same thing can happen here in Jamaica, perhaps is happening right now to some poor soul's pension money as we speak. We have our fair share of people who believe that they know better but who can't be found when it is time to reckon up and take account of their stewardship. But I can assure you of one thing: if you participate, it won't happen to you.

I look at the efforts of this plan and of your trustees to inform its members. I see here today an example of the response, the interest in participation, and I am very much encouraged about the future for pension funds in Jamaica if your example is followed by others. I can look forward to working with the persons here infused with the spirit of the reform and I can commit to support them in their efforts to protect your financial future.

Thank you.

Brian Wynter  
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