

Attachment 1

BANK INDONESIA CIRCULAR LETTER

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CONCERNING

IMPLEMENTATION OF ANTI-FRAUD STRATEGY FOR COMMERCIAL BANKS

GUIDELINE FOR IMPLEMENTATION OF ANTI-FRAUD STRATEGY
FOR COMMERCIAL BANKS

I. BACKGROUND

1. In the framework of preventing the occurrences of cases of operational deviations in the banking sector, specifically frauds, which could bring losses to customers or Bank, it is necessary to enhance effectiveness of the internal control, as an effort to minimize the risks of frauds through the implementation of anti-fraud strategy.
2. Up until this time, either directly or indirectly, the implementation of fraud prevention has been undertaken by Bank, among others through the application of Risk Management, particularly the internal control system, and the implementation of good corporate governance. However, in order for the implementation to be effective, there is still a need to make stepped-up efforts to ensure that fraud prevention becomes the focus of attention and culture at Bank in overall aspects of the organization, both the management as well as the employees.
3. Effectiveness of the fraud control in business processes is the responsibility of management, and as such, the management needs to have proper and comprehensive understanding concerning fraud to enable it to give directions and foster awareness for fraud risk control at the Bank.
4. Anti-fraud strategy is the manifestation of Bank management commitment in controlling fraud, which is implemented in the form of fraud control system. This strategy demands that management uses resources to enable the fraud control system be implemented in an effective and sustainable manner.
5. Guideline for the implementation of anti-fraud strategy in this regulation directs Bank in the undertaking of fraud control through efforts that aim not only at prevention but also detection and investigations as well as improvement of the system as part of the strategy that is integral in fraud control.

II. GENERAL GUIDELINE IN IMPLEMENTATION OF ANTI-FRAUD STRATEGY

1. In this guideline, fraud means a deviating act or a purposeful neglect undertaken in order to deceive, cheat, or manipulate Bank, customer, or another party, that occurs inside the Bank and/or using Bank's facility so as to cause the Bank, customer, or another party to suffer a loss and/or to cause the fraudster to gain a financial benefit, both directly as well as indirectly.

Types of actions that are categorized as frauds are deceptions, swindles, embezzlements of assets, leakages of information, banking crimes (tipibank), and other similar actions.

2. Anti-fraud strategy is Bank strategy in controlling frauds that is designed by making reference to the processes related to the occurrences of frauds, by taking into consideration the characteristics and extent of potential of frauds, that is developed in a comprehensive and integral manner and implemented in the form of fraud control system. Implementation of the anti-fraud strategy constitutes part of application of Risk Management, particularly in regard of the aspect of internal control system.
3. Success of the overall implementation of the anti-fraud strategy very much depends on an environment that supports the materialization of conducive condition so that all related parties can play their roles well in the implementation of the fraud control system.
4. Structure of the anti-fraud strategy wholly combines the basic principles of Risk Management, specifically the internal control and good corporate governance. Implementation of the anti-fraud strategy in the form of fraud control system is broken down into 4 (four) pillars of fraud control strategies that are inter-related, namely: (i) prevention; (ii) detection; (iii) investigation, reporting, and sanction; (iv) as well as monitoring, evaluation, and follow-up.

III. APPLICATION OF RISK MANAGEMENT

Implementation of anti-fraud strategy as part of the implementation of Risk Management application cannot be separated from the scope of Risk Management application in general. Therefore, effectiveness of the implementation of anti-fraud strategy needs at least be supported by strengthening the aspects of Risk Management that focus on fraud control. These aspects cover at least management's active

supervision, organization structure and accountability, as well as control and monitoring. The minimum scope of each of these supporting aspects is as follows:

1. Management's active supervision

Management's active supervision on frauds covers matters that are the authority and responsibility of management, both Board of Commissioners as well as Board of Directors.

These authorities and responsibilities cover at least the following:

- a. development of anti-fraud culture and awareness at all organization levels, which among others covers declaration of anti-fraud statement and adequate communication to all levels of the organization concerning behaviors that are included as fraudulent actions.
- b. development and supervision of the implementation of code of conduct related to the prevention of frauds for all levels of the organization;
- c. development and supervision of the implementation of overall anti-fraud strategy;
- d. development of human resource quality, particularly related to enhancement of the awareness and control of frauds;
- e. monitoring and evaluation of fraudulent incidents as well as determination of follow-up actions; and
- f. development of effective communication channel at internal Bank so that all Bank officers/employees understand and comply with prevailing policies and procedures, including policies related to the control of frauds.

2. Organization Structure and Accountability

In supporting the effectiveness of the implementation anti-fraud strategy, Bank is obliged to establish a unit or function that has the task of handling the implementation of anti-fraud strategy. Matters that require attention in the establishment of this unit or function include at least the following:

- a. the establishment of the unit or function within the organization structure shall be suited to the characteristics and complexity of Bank business activities;
- b. determination of clear details of tasks and responsibilities;

- c. that unit or function shall be directly responsible to the President Director and its communication and reporting lines shall be directly to the Board of Commissioners; and
- d. implementation of the tasks of this unit or function shall be undertaken by human resources who have the competency, integrity, and independency, as well as is supported by clear accountability.

3. Control and Monitoring

In undertaking control and monitoring, Bank is obliged to undertake steps that focus on enhancement of the effectiveness of the anti-fraud strategy implementation. These steps shall include at least the following:

- a. Determination of control policies and procedures that aim specifically at fraud control;
- b. Control through review by management (top level review) as well as review of operations (functional review) by the Internal Audit Work Unit on the implementation of anti-fraud strategy.
- c. Control in the field of human resources aims at enhancement of the effectiveness of the implementation of tasks and fraud control, such as, rotation policy, movement policy, obligatory leave, and social activities or gatherings;
- d. Determination of segregation of duties in the implementation of Bank activities at all levels of the organization, for example, implementation of four eyes principle in credit extension activities with the aim that each party related to these activities does not have the opportunity to commit and hide frauds in the execution of tasks;
- e. information system control that supports electronic data processing, retention, and security in order to prevent the potential occurrences of frauds. Also in regard of data security, Bank is obliged to have an adequate contingency program. This information system control needs to be supplemented with the availability of accounting system to ensure the use of data that is accurate and consistent with Bank financial recording and reporting, among others through periodic data reconciliations or verifications; and
- f. other controls in the framework of fraud control, such as control of physical assets and documentation.

IV. ANTI-FRAUD STRATEGY

Anti-fraud strategy, which is developed in a comprehensive and integral manner and is implemented in the form of fraud control system, is implemented by using instruments that comprise the details of 4 (four) inter-related pillars as follows:

1. Prevention

The prevention pillar contains instruments aimed at reducing the potential occurrences of frauds that cover at least:

a. Anti-Fraud Awareness

Anti-fraud awareness is an effort to develop awareness concerning the importance of fraud prevention by all related parties.

Good leadership supported by high anti-fraud awareness is expected to foster the growth of awareness of all elements at Bank concerning fraud control.

Good moral value and awareness of management concerning anti-fraud should inspire each policy or regulation determined.

Efforts to develop anti-fraud awareness are undertaken among others through:

1) Development and socialization of Anti-Fraud Statement.

For example: policy of zero tolerance towards frauds.

2) Employee awareness program

For examples: the holdings of seminars or discussions related to anti-fraud, trainings and publications concerning understanding of various forms of frauds, transparency on results of investigations, follow-up actions on frauds that are undertaken in a sustainable manner.

3) Customer awareness program

For examples: development of anti-fraud brochures, written explanations or through other media to enhance awareness and alertness of customers/depositors of potential incidents of frauds.

b. Identification of Vulnerability

Identification of vulnerability is a Risk Management process in identifying, analyzing, and evaluating risk potential of incidents of frauds.

In general, identification of vulnerability aims at the identification of the risk potential of incidents of frauds, which is inherent in each activity that has the potential to bring losses to Bank.

Bank is obliged to undertake identification of vulnerability on each activity. Results of identifications shall be documented and informed to parties that have interests and all the time updated particularly on activities that are deemed to have high risk of incidents of frauds.

c. Know Your Employee

As an effort to prevent frauds, the know your employee policy constitutes an effort for control from the aspect of human resources. The Bank's know your employee policy shall cover at least:

- 1) Effective recruitment system and procedure. This system expects to find a complete and accurate picture of the track records of candidate employees (pre employee screening);
- 2) selection system that is supplemented with proper qualifications and taking into consideration the risks, as well as determined in an objective and transparent manner. This system must include the implementation of promotions as well as movements, including placements in positions that have high risk against frauds; and
- 3) know your employee policy covers among others knowing and monitoring the characters, behaviors, and life styles of employees.

2. Detection

The detection pillar contains instruments aimed at the identification and finding of incidents of frauds, which cover at least:

a. Whistleblowing Policy and Mechanism

This policy is aimed at enhancing the effectiveness of fraud control system implementation with a stress on disclosures of claims.

The whistleblowing policy must be formulated such that it is clear, easily understood, and could be implemented effectively so as to bring encouragement and awareness to Bank employees and officers to report frauds that have occurred. To enhance effectiveness of the whistleblowing policy implementation, this policy shall cover at least:

1) Protection for Whistleblowers

Bank must have a commitment to provide support to and protection for each reporter of fraud as well as guarantee the secrecy of the identity of the reporter of fraud and fraud report submitted.

2) Regulation related to Fraud Reporting

Bank must develop an internal regulation concerning the reporting of frauds by making reference to prevailing regulations and legislations.

3) System for Reporting and Follow-Up Mechanism for Fraud Reporting

Bank must develop an effective system for fraud reporting, which contains clarity on reporting process, which is among others related to procedure, media, and responsible party to handle reporting. The reporting system must be supported with clarity on the follow-up mechanism for fraud incidents reported.

The policy should be transparent and consistently implemented so as to induce trust in all Bank employees in the reliability and secrecy of the whistleblowing mechanism.

b. Surprise Audit

The policy and mechanism of surprise audit must be applied, particularly on business units that have high risk or are vulnerable to the occurrence of frauds. Implementation of surprise audit could increase employees' alertness in executing their tasks.

c. Surveillance System

The surveillance system is an action of testing or investigation without being known or recognized by the party being tested or investigated in the framework of monitoring and testing the effectiveness of the anti-fraud policy. The surveillance system could be undertaken by an independent party and/or Bank internal party.

3. Investigation, Reporting, and Sanction

The investigation, reporting, and sanction pillar contains instruments aimed at investigation of information, reporting system, including imposition of sanctions on incidents of frauds in Bank business activities, which cover at least:

a. Investigation

An investigation is undertaken by collecting evidence related to an event that is reasonably suspected to have been event of fraudulent action.

Investigation is an important part in the fraud control system, which brings a message to each related party that each indication of fraudulent action that is detected will always be processed in accordance with prevailing

investigation standards and the fraudsters will be processed in accordance with prevailing regulations.

Bank investigation standards shall cover at least:

- 1) determination of the party authorized to undertake investigations by taking into consideration the required independency and competency; and
- 2) mechanism for execution of investigations in the framework of following up results of detections by maintaining the secrecy of information obtained.

b. Reporting

Bank is obliged to have an effective reporting mechanism for the execution of investigations and events of fraud found. The reporting mechanism covers reporting to Bank internal management as well as Bank Indonesia.

c. Imposition of sanctions

Bank is obliged to have an effective internal policy on imposition of sanctions in the framework of following up results of investigation so as to induce a deterrent effect on the fraudsters. This policy shall contain at least the following :

- 1) mechanism for imposition of sanctions; and
- 2) party authorized to impose sanctions.

The policy on imposition of sanctions must be implemented in a transparent and consistent manner.

4. Monitoring, Evaluation, and Follow Up

The monitoring, evaluation, and follow up pillar contain instruments aimed at the monitoring and evaluation of events of frauds as well as required follow up actions based on results of evaluations, which contain at least:

a. Monitoring

One of the important steps in the implementation of fraud control system is the monitoring of follow up actions undertaken in relation to fraud incidents, in accordance with Bank internal regulation as well as prevailing regulations and legislations.

b. Evaluation

To support the implementation of evaluation, Bank needs to maintain data on fraud events (fraud profiling). Data of those events could be used as a tool for evaluation. Data of those fraud events shall at least cover data and information as referred to in Attachment 2.

Fraud event data and results of evaluations would enable identification of weaknesses and causes for the occurrences of frauds as well as determination of required steps for improvement, including strengthening of the internal control system. Overall evaluation of the fraud control system needs to be performed periodically.

c. Follow Up

Bank is obliged to have a follow up mechanism that is based on results of evaluations of fraud incidents in order to improve weaknesses and strengthen the internal control system to enable prevention of reoccurrence of the frauds due to similar weaknesses.

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