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## United Nations Commission on International Trade Law

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## Indicators of Commercial Fraud

### Note by the Secretariat\*

At its thirty-fifth session in 2002, the Commission first considered whether the problem of fraudulent practices of an international character resulted in a significant adverse economic impact on world commerce and negatively affected legitimate commercial institutions. At its thirty-sixth session in 2003, the Commission considered the note of the Secretariat (A/CN.9/540), and agreed with the recommendation that an international colloquium should be organized to permit an exchange of views from various interested parties regarding the private law aspects of commercial fraud. At its thirty-seventh session in 2004, the Commission considered the report of the UNCITRAL Secretariat on the colloquium (A/CN.9/555), and, *inter alia*, agreed that, with a view towards education, training, and prevention, the preparation of materials setting out common features present in typical fraudulent schemes could be useful as educational material for participants in international trade and other potential targets of perpetrators of fraud, in order to help potential targets protect themselves and avoid becoming victims of fraudulent schemes. It was agreed that the Secretariat should consider preparing, in close consultation with experts, such materials listing common features present in typical fraudulent schemes. The annex attached to this note is the result of that work, and is presented to the Commission for its consideration. Due to the length of the materials, they have been separated into three documents that should be read together: A/CN.9/624; A/CN.9/624/Add.1 and A/CN.9/624/Add.2.

Bearing in mind the full agenda of the current session of the Commission, one possible course of action may be for the Commission to take note of the text and, with any comments it may wish to make, request the Secretariat to disseminate it to Governments and potentially interested institutions, in particular international intergovernmental and non-governmental organizations, with a view to obtaining comments. On the basis of the comments received, the Commission would be able to assess any other action it may wish to take in respect of it.

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\* This note is submitted late due to the need to complete consultations and finalize subsequent amendments.



**Annex****UNCITRAL Commercial Fraud Project****RECOGNIZING AND PREVENTING COMMERCIAL FRAUD****Indicators of Commercial Fraud****Contents**

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## I. Introduction

### Purpose and Target audience

As early as 2002, the United Nations Commission on International Trade Law (UNCITRAL) first considered the problem of fraudulent practices that resulted in a significant adverse economic impact on world commerce and negatively affected legitimate commercial institutions. Through a series of consultations with experts and government officials who regularly encounter and combat commercial fraud and who represented different regions, perspectives, and disciplines, UNCITRAL became aware of the widespread existence of commercial fraud and its significant worldwide impact, regardless of a country's level of economic development or system of government. In considering possible responses to this threat, it was felt that education and training could play significant roles in fraud prevention, and that the identification of common warning signs and indicators of commercial fraud could be particularly useful in combating fraud.

To this end, the UNCITRAL secretariat met over the ensuing years with international experts and government officials knowledgeable in the identification and prevention of commercial fraud, and as a result developed the attached list of twenty-three indicators of commercial fraud. The overall objective of this project was to assist in the prevention of commercial fraud by creating an easily understood and widely-disseminated document that set out indicators to assist potential victims and their organizations in the identification of behaviour that could be associated with or could constitute commercial fraud. Governments and other bodies and organizations are encouraged to disseminate these materials as widely as possible, and encourage their use in the prevention of fraud.

It is hoped that, in addition to preventing the perpetration of specific commercial frauds through education and awareness, this anti-fraud project will serve three main overarching purposes. First, these materials are intended to identify patterns and characteristics of commercial fraud in a manner that facilitates the private sector in combating commercial fraud in an organized and systematic manner. Second, it is hoped that governmental bodies may be assisted by these materials in understanding how to help the public and private sector to address the problem of commercial fraud. Finally, these materials may assist the criminal law sector in understanding how best to engage the private sector in the battle against commercial fraud.

The intended audience for these materials includes individuals, professionals, business persons, regulators, law enforcement officers, litigants, and potentially arbitration tribunals and courts in cases involving commercial fraud. These materials are not intended as a legislative text nor a legal text, but rather as instructive materials containing useful guidance and reference materials for users. It is hoped that financial decision-makers and those charged with combating commercial fraud can learn and benefit from these materials, be they individual investors or purchasers, CEOs, bank executives, law enforcement agencies or regulators, or the board of directors of any company, large or small. Even decision-makers charged with distributing emergency relief or crisis funds on behalf of governments or international organizations may benefit from recognizing and remaining alert to these potential indicators of fraud. In addition, third parties such

as employees of banks or other entities, or professionals assisting in a transaction or an investment, must be aware that they may unwittingly assist in the perpetration of a fraud by simply being blind to the indicators of a potential fraud.

Examination of the various indicators has revealed that they tend to be present in many different cases of potential fraud, regardless of the level of sophistication of the financial decision-maker, or of the development of a particular economy involved. In an effort to illustrate this point, the instances and examples that are given in these materials for each of the indicators are drawn from various different areas of legal practice and include various different types of victims. They are intended to demonstrate that the indicators are meant to be of universal application in a commercial and administrative context, regardless of the identity or role of the potential victim, their net worth, their level of sophistication or their geographic location. The only quality that the victims are certain to share is a vulnerability to fraud that stems from their role as a financial decision maker.

However, it is important to remember that each of the indicators taken alone or in combination is not intended to definitively indicate the presence of commercial fraud. Instead, the presence of a single warning sign is intended to send a signal that commercial fraud is a possibility, while the presence of several of the indicators should heighten that concern.

The presentation of each of the indicators is similar: first, the indicator is identified, followed by a more detailed description of the indicator, which is in turn followed by instances and examples of the particular indicator as found in a commercial fraud in a variety of different contexts. Advice is then provided regarding what may be done to avoid or to counteract the effects of the behaviour identified in each indicator, as appropriate. Finally, since the identification of discrete indicators is not conducive to a scientific exercise with clear demarcations between them, many of the indicators may or should overlap, and these materials include cross references to other related indicators, where relevant.

### History

At its thirty-fifth session in 2002, UNCITRAL first considered whether the problem of fraudulent practices of an international character resulted in a significant adverse economic impact on world commerce and negatively affected legitimate commercial institutions. It was felt that fraudulent practices that affected international commerce had not been sufficiently addressed by international bodies, particularly with respect to their commercial aspects. It was suggested that UNCITRAL was well-positioned to consider the issue of commercial fraud, since it presented the unique combination of a governmental perspective with recognized expertise in international commerce and a tradition of collaboration with other international organizations.<sup>1</sup>

In order to assess the extent and implications of commercial fraud and to consider possible recommendations regarding future action, in December 2002, the UNCITRAL Secretariat convened a meeting of experts who regularly encounter and combat commercial fraud and who represented different regions, perspectives, and disciplines. Following that meeting, the UNCITRAL secretariat prepared and issued a note on possible future work relating to commercial fraud (A/CN.9/540) as

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<sup>1</sup> *Official Records of the General Assembly, Fifty-seventh Session, Supplement No. 17 and corrigendum (A/57/17 and Corr.3)*, paras. 279-290.

requested by UNCITRAL at its thirty-fifth session. The note concluded that available evidence suggested that commercial fraud constituted a serious and potentially increasing threat to international commerce. The note also considered factors in defining or describing commercial fraud, concluding that a precise definition was not currently available but that it would be useful to identify and detail common patterns of fraudulent commercial conduct. Finally, the note also suggested that there was an important independent commercial dimension to commercial fraud in addition to that of criminal law enforcement, and made several recommendations to UNCITRAL in regard to future work.

At its thirty-sixth session in 2003, UNCITRAL considered the note of the Secretariat (A/CN.9/540). It agreed with the recommendation that an international colloquium should be organized to permit an exchange of views from various interested parties, including those working in national Governments, intergovernmental organizations and relevant private organizations on the private law aspects of commercial fraud. It was also noted that the colloquium would provide an opportunity to promote an exchange of views with the criminal law and regulatory sectors that combat commercial fraud and to identify matters that could be coordinated or harmonized.<sup>2</sup>

A colloquium on international commercial fraud was held in Vienna from 14 to 16 April 2004. The speakers, panellists, and participants at the colloquium consisted of experts from each of several legal practice areas examined, representing as broad a spectrum of approaches to the problem of commercial fraud as possible, and included approximately 120 participants from 30 countries. It was agreed at the colloquium that any doubt had been dispelled as to the widespread existence of commercial fraud and its significant worldwide impact, regardless of a country's economic development or system of government. It was also agreed that education and training played significant roles in fraud prevention and that it would be particularly useful to identify common warning signs and indicators of commercial fraud. In addition, it was agreed at the colloquium that local cooperative efforts between law enforcement bodies and the private sector seemed particularly effective and should be encouraged (see A/CN.9/555, paras. 3, 4, 25-28, and 62-71).

At its thirty-seventh session in 2004, UNCITRAL considered the report of the UNCITRAL secretariat on the colloquium (A/CN.9/555), and, inter alia, agreed that, with a view towards education, training, and prevention, the preparation of materials setting out common features present in typical fraudulent schemes could be useful as educational material for participants in international trade and other potential targets of perpetrators of fraud. It was thought that such materials would help potential targets protect themselves and avoid becoming victims of fraudulent schemes. Further, it was thought that national and international organizations interested in fighting commercial fraud could be invited to circulate such material among their members in order to help test and improve those lists. While it was not proposed that UNCITRAL itself or its intergovernmental working groups be directly involved in that activity, it was agreed that the UNCITRAL Secretariat should consider preparing, in close consultation with experts, such materials listing common features present in typical fraudulent schemes.<sup>3</sup>

<sup>2</sup> Ibid., *Fifty-eighth Session, Supplement No. 17* (A/58/17), paras. 240-241.

<sup>3</sup> Ibid., *Fifty-ninth Session, Supplement No. 17* (A/59/17), paras. 110-112.

At its thirty-eighth session in 2005, UNCITRAL reiterated its support for this project,<sup>4</sup> and at its thirty-ninth session in 2006, UNCITRAL further approved of the general approach taken in the drafting of these materials as set out in a note by the Secretariat (A/CN.9/600).<sup>5</sup>

For further information, please visit the UNCITRAL website at [www.uncitral.org](http://www.uncitral.org).

## II. What is Commercial Fraud?

It would not be appropriate to set out a strictly legal definition of commercial fraud in light of the aims and objectives of these materials, nor would such a definition allow sufficient flexibility for the intended broad use of those materials. However, a descriptive definition outlining the main elements of commercial fraud could be helpful to the user of these materials.

The following elements are key to the identification of commercial fraud:

- (1) There is an element of deceit or of providing inaccurate, incomplete or misleading information;
- (2) Reliance on the deceit or the information provided or omitted induces the target of the fraud to part with some valuable thing that belongs to the target or to surrender a legal right;
- (3) There is a serious economic dimension and scale to the fraud;
- (4) The fraud uses or misuses and compromises or distorts commercial systems and their legitimate instruments, potentially creating an international impact; and
- (5) There is a resultant loss of value.

Further, the term “fraudster” has been used in these materials as a term to identify someone who is perpetrating, or attempting to perpetrate a fraud.

## III. Related Topics

A number of serious issues related to commercial fraud have not been covered in these materials in order to keep them of a manageable and useful size, and since such issues have been, and are continuing to be, dealt with in other fora or by other organizations. A non-exhaustive list of such issues, and some suggestions regarding where further information can be found, appears below. Note also that the suggested sources for further information are limited to international organizations, and that there are numerous national governmental and non-governmental organizations which have also worked extensively in these areas, and to which resort should be had for more information.

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<sup>4</sup> Ibid., *Sixtieth Session, Supplement No. 17* (A/60/17), para. 220.

<sup>5</sup> Ibid., *Sixty-first Session, Supplement No. 17* (A/61/17), para. 217.

## **A. Corruption and Bribery**

Corruption has been defined by Transparency International as “the misuse of entrusted power for private gain”. Further differentiation has been made between “according to the rule corruption” and “against the rule corruption”, wherein the former includes facilitation payments, where a bribe is paid to receive preferential treatment for something that the receiver of the bribe is required to do by law, while the latter includes bribes to obtain services that the receiver of the bribe is prohibited from providing.

A number of international organizations have adopted instruments, including conventions, aimed at fighting corruption and bribery. These organizations include: the United Nations; the African Union; the Council of Europe; the European Union; the Economic Community of West African States; the Organization of American States; and the Organisation for Economic Cooperation and Development.

There is a large amount of information available concerning corruption and bribery, including materials on how to combat it. The following lists a few of the many sources of such information:

- Transparency International; [www.transparency.org](http://www.transparency.org)
- United Nations Office on Drugs and Crime; [www.unodc.org](http://www.unodc.org)
- Organisation for Economic Cooperation and Development; [www.oecd.org](http://www.oecd.org)
- Organization of American States; [www.oas.org](http://www.oas.org)
- The World Bank; [www.worldbank.org](http://www.worldbank.org)

## **B. Money-Laundering**

Money-laundering may be described as the practice of engaging in specific financial transactions in order to conceal the identity, course, and/or the destination of money. A number of national and international rules and programmes have been developed to combat money-laundering.

Again, there is a great deal of information available on money-laundering, both nationally and internationally. For example, resort may be had to:

- Financial Action Task Force; [www.fatf-gafi.org](http://www.fatf-gafi.org)
- International Bar Association Anti-Money-Laundering Forum; [www.anti-moneylaundering.org](http://www.anti-moneylaundering.org)

## **C. Transparency**

“Transparency” has been defined, again by Transparency International on their website, as “a principle that allow those affected by administrative decisions, business transactions or charitable work to know not only the basic facts and figures, but also the mechanisms and processes” by means of which the decisions were made and transactions entered into. It is further said that “it is the duty of civil servants, managers and trustees to act visibly, predictably and understandably”.

As a general principle, true transparency should be sought in all transactions and if achieved, should result in the prevention and avoidance of commercial fraud.

For further information, one source that may be consulted is:

- Transparency International; [www.transparency.org](http://www.transparency.org)

## **D. Best Practices**

“Best practices” are, in this case, those techniques, methods, processes, activities or the like, used by highly respected organizations, public and private, that are focused on the prevention or detection of commercial fraud, and that should be adopted by entities such as companies and financial institutions and consistently followed by their employees. If such approaches are followed, and the proper processes, checks and testing have taken place, those systems should assist greatly in the prevention or detection of a fraud. Entities and organizations should be sure to investigate and adopt the best practices most suited to their operations, and should investigate them by way of their professional organizations or consult with private sector specialists.

### **(1) Corporate Governance**

The term “corporate governance” is the set of processes, laws, policies and institutions affecting the way a corporation is directed, administered and controlled, and involves the set of relationships between the company’s management, its board of directors, its shareholders and other stakeholders. At the core of corporate governance are issues such as corporate fairness, transparency, fiduciary duty and accountability.

Establishing and adhering to the principles of good corporate governance should assist greatly in the prevention of commercial fraud either on the company, or on other parties, with the assistance of employees.

A great deal of material has been published on this topic, and resort could be had to the following sources:

- Organisation for Economic Cooperation and Development; [www.oecd.org](http://www.oecd.org)

### **(2) Whistleblower policies**

A “whistleblower” is someone, usually an insider, who reveals wrongdoing within an organization to the public or to those in positions of authority. Whistleblowing policies operate to give adequate protection to those who wish to come forward to report deviations from legal or ethical corporate standards. This can be done, for example, via confidential telephone services or intranet sites through which employees and business partners can address concerns or pass information. To make such services effective, genuine concerns must be listened to and acted upon in a timely manner by the responsible board committee.

The adoption of adequate whistleblower policies by an organization, and education of employees about the existence and anonymity of such processes, can aid greatly in the detection of fraud or wrongdoing within an organization.



Again, much has been written on this topic, for example by:

- Transparency International; [www.transparency.org](http://www.transparency.org)

### (3) Role of Internal and External Auditors

Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes. Internal auditors are employees of the entity who report to a general or chief auditor, who, in turn, reports to the Audit Committee of the Board of Directors.

An external auditor consists of audit professionals who perform an audit on the financial statements of a company, individual or other organization, its key characteristic being that it is independent from the entity being audited. The external auditor also reports to the Board of Directors of an organization, and may also be required by specific legislation to make submissions to regulatory agencies.

Both types of audits are useful and recommended to detect fraudulent activity and to assist in its prevention.

Again, reference may be had to:

- Transparency International; [www.transparency.org](http://www.transparency.org)
- Organisation for Economic Cooperation and Development; [www.oecd.org](http://www.oecd.org)

### **Indicators of Commercial Fraud**

Indicator 1	Irregular Documents
Indicator 2	Misuse of Technical Terms
Indicator 3	Inconsistencies in the Transaction
Indicator 4	Misuse of Names
Indicator 5	Disproportionate Returns
Indicator 6	Undue Secrecy
Indicator 7	Overly Complex or Overly Simplistic Transactions
Indicator 8	Frustration of Due Diligence
Indicator 9	Corrupted Incentives
Indicator 10	Ensnarement and Psychological Inducements
Indicator 11	Crisis-Caused Breakdowns in Preventive Controls
Indicator 12	Immediate, Fast or Irrevocable Transfer of Funds
Indicator 13	Questionable or Unknown Source of Repayment
Indicator 14	Irrational or Illogical Aspects or Explanations
Indicator 15	Fraud Based on Abuse of Personal Affinity or Relationships

Indicator 16	Fraud By or Involving Employees
Indicator 17	Unusual Involvement or Participation of Professionals
Indicator 18	Inappropriate Requests for Information Disclosure
Indicator 19	Unsolicited E-mails and Related Misuse of Technology
Indicator 20	Pyramid and Multi-Level Marketing Schemes
Indicator 21	Frauds involving Goods and Services
Indicator 22	Securities Fraud and Market Abuse
Indicator 23	Misuse of Insolvency Proceedings

**Indicator 1: Irregular Documents**

Commercial frauds almost always involve the issuance of, use of, or reliance on documents that are not normally or typically used in the type of transaction to which they are intended to relate, or on documents that contain discernable irregularities either individually, or when read in light of all the documents presented in support of the scheme.

**Explanation:**

Commercial frauds, like legitimate transactions, involve the use of multiple documents to explain, memorialize, and reflect the transaction. However, the documents used in commercial frauds often differ from those used in legitimate transactions either because they are improperly drafted, or because they contain some unusual features to induce investment, to bolster the fraudster's credibility, to explain the extraordinary returns claimed by the fraudster, or they set out unusual procedures. It is often possible to determine the likelihood or presence of a commercial fraud by identifying these irregular aspects. Documents used in support of a commercial fraud can be genuine, fraudulent, forged, or fictitious, and can be issued or authenticated either properly or improperly by institutions or individuals. Sometimes professionals can be involved in their creation or authentication.

**Instances and Examples:**

- Documents that may be used in connection with commercial frauds include:

- Genuine documents;

Illustration 1-1: Such documents may include: studies by organizations; letters of introduction; written attestations that an individual has an account in the institution or is a customer of the institution; a contract drafted by a lawyer; an authenticated telecommunication or funds transfer or SWIFT.

- Fictitious documents that are not used in legitimate commerce;

Illustration 1-2: Such documents may include: an "irrevocable SWIFT"; "UCP500 Forfait Transaction" or "Grain Warrants".

- Forged or fraudulent documents;

Illustration 1-3: An employee forges the signature of a bank manager on a letter provided by the fraudster.

Illustration 1-4: Documents that are commonly forged or fraudulent may include a forged signature or misdescription of goods on a bill of lading; a bank guarantee; documents under a commercial letter of credit; or false audit reports.

- Counterfeits of genuine documents.

Illustration 1-5: Documents that are commonly counterfeited include stock certificates; debentures; promissory notes; precious metal depositary certificates; warehouse certificates; or government procurement contracts, all of which may be used to induce investment in a fraudulent investment scheme or hypothecated to obtain an extension of credit from a legitimate financial institution.

- Legitimate institutions or their employees can be knowingly or unwittingly induced to issue or verify legitimate or illegitimate documents that are then used to enhance the fraudulent scheme. Electronic verification may also be requested.

Illustration 1-6: A clerk is asked to issue or authenticate a document that is not usually issued by that clerk or by that institution. Or, the requester of the document seeks the inclusion of unusual phrases such as that funds are of “non-criminal origin”, or may request the insertion of legitimate commercial terms such as that the customer is “ready, willing, and able” to enter into transaction. The clerk obliges in order to assist the customer but without understanding the document or phrases, and the documents are subsequently used to bolster the credibility of the fraud.

Illustration 1-7: A clerk authenticates a document prepared by a customer on bank or company stationery. Although the clerk intends only to authenticate the signature or identity of the customer, the document contains statements that are used to enhance credibility by indicating that the bank or company attests to what is said in the document.

- The irregularities in documents used in commercial fraud may be caused by or connected with professionals.

Illustration 1-8: A lawyer, accountant or other professional prepares documents at the request of a client regarding a transaction that the professional does not inquire into or does not understand, and that does not make economic or other sense. The fraudster often needs the professional to give credibility to his or her scheme. Agreeing to witness or confirm a pre-signed document would be a particular example of a transaction that could facilitate a fraud.

- A commercial fraud may be signalled by:
  - An absence of proper documentation;

Illustration 1-9: The existence of only a few poorly drafted documents for a major transaction; or a bank loan without a business plan to repay money.

- Documents that are issued by a genuine commercial entity but contain irregularities in connection with their issuance;

Illustration 1-10: A shipping clerk is asked to sign and postdate a document stating that goods, which have not yet arrived, have been received on the basis of the presenter's representation that goods will be received by that date. The presenter then uses the document to obtain payment, although goods are never delivered.

Illustration 1-11: A seller of real or personal property is asked to adjust the stated purchase price for real or personal property so that the buyer may increase the amount able to be borrowed or to decrease tax liability for the transaction or the property.

- Internal irregularities and inconsistencies in the documents;

Illustration 1-12: A document relating to a sophisticated transaction or one for a large sum contains spelling errors or grammatical errors, or has unprofessional-looking graphics or an unsophisticated appearance.

Illustration 1-13: Odd phrases or terms found in genuine documents, including: "NC/ND"; a document that is not a letter of credit is said to be subject to UCP500; performance in a "year and a day" or "a month and a day"; reference to "international banking seconds, hours or days".

Illustration 1-14: A transaction for a large amount of money that is disproportionate with the situation or the person with which it is connected, such as a small bank with assets of UK £75 million issuing a document for UK £100 million.

- The presence of a document that does not itself make sense or that does not make sense in connection with other documents involved in the transaction;

Illustration 1-15: In a transaction allegedly involving the sale of independent guarantees, a document was presented relating to factoring.

- The presence of incorrect or unusual headings of or in documents;

Illustration 1-16: What is supposed to be a letter of credit is entitled "Hypothecation Agreement" and contains a promise to pay funds to bearer.

- Documents that do not appear in the normal course of business;
- The unusual appearance or texture of a financial instrument;

Illustration 1-17: Document contains blurred typography, poor paper quality, spelling mistakes or an unprofessional look or graphics.

- The antedating or postdating of documents;

Illustration 1-18: A bill of lading stating that the goods are loaded on board a vessel is issued with a date a week earlier than the date the goods are said to have been loaded.

- Or changes in the existing documentation that fundamentally and inexplicably change the nature of the transaction.

Illustration 1-19: The transaction is said to relate to trading in sugar and, purportedly as a result of a difficulty, the documents are suddenly switched to relate to a sale of steel.

Illustration 1-20: The documentation was an independent guarantee and it is suddenly a promissory note.

#### **Advice:**

- Complete documentation of the investment should be required in advance and any unusual characteristics or aspects that are not understood in the form, content, or authenticity of the documents should be investigated, especially where the investment involves financial instruments.
- Read carefully documents presented in support of an investment and remember that they should be consistent in terms of the transaction as a whole.
- Documents should not be antedated or postdated, and the dates referred to in them should be consistent.
- Documents presented in support of a proposed commercial transaction should not be relied upon without considering their content, purpose and source.
- Inquire whether the document is of a type that is regularly issued.
- A general addressee, such as “To whom it may concern” should be cause for further inquiry.
- Do not assume the authenticity of letterheads of well-known companies or organizations that could have been produced by laser printer.
- Verify signatures.
- Determine that professionals employed have an understanding of the documents they are preparing or verifying.
- Perform thorough due diligence by consulting independent sources of information, or by consulting legal and risk management or security departments regarding the documents and their contents.
- If critical reliance in a transaction is placed on a particular document, it should be produced.
- Extreme caution should be exercised if engaging in a transaction where irregular or incomplete documents are used or relied upon as a matter of course in the trade.
- Never grant power of attorney to persons unknown.

- Do not sign, issue or authenticate documents that are unusual, that are not understood, that are not usually signed by the individual or institution being requested to sign them, or whose purpose is not understood.
- Do not sign a document that is incomplete or that is in another language that is not understood.
- Never sign or issue a statement that is known or suspected to be untrue.
- Investigate whether the person requesting the service is a regular customer.
- It may be advisable to set out the purpose for which the document was prepared in the body of the document itself, as a means to possibly avoid later misuse.
- Be cautious of issuing unusual documents, particularly when the text is provided by the requester.
- Use forms that are approved by legal and risk management or security departments.
- If presented with a financial instrument that is unfamiliar in the marketplace, such as a stock certificate traded on a foreign exchange, have the document examined by a reputable expert in the field, like a stockbroker of good reputation.

**See also:** Indicator 3 – Inconsistencies in the Transaction; Indicator 4 – Misuse of Names; Indicator 6 – Undue Secrecy; Indicator 8 – Frustration of Due Diligence; and Indicator 17 – Unusual Involvement or Participation of Professionals; Addendum 1 – Performing Due Diligence.

#### **Indicator 2: Misuse of Technical Terms**

Commercial frauds misuse technical terms by using an actual term in an incorrect context or inventing an impressive sounding term to gain credibility, to obscure implausible aspects of the scheme, or to impress or intimidate victims or their advisors.

#### **Explanation:**

Modern commerce and finance are complex and regularly use specialized terms related to a transaction or its financing. Commercial frauds frequently employ such terms to give the impression that the scheme is genuine, to impress or intimidate victims, or to cover their inability to explain inconsistencies or illegal aspects of the transaction. Since the fraudsters are often not knowledgeable themselves, they often misuse specialized terms, thereby signalling that the transaction is not genuine. Legitimate transactions occasionally may contain mistakes that are not essential to the transaction, and where a misuse is infrequent or the mistake is peripheral to the nature of the scheme, it is less likely to indicate commercial fraud. However, where the misuse is of a term essential to the scheme, and where it is consistent and frequent, it may indicate that the transaction is not legitimate.

#### **Instances and Examples:**

- Technical terms can be misused to:

- Impress or overwhelm the victim;

Illustration 2-1: Fraudster gives a detailed but distorted discussion of macroeconomic history oriented towards reinforcing the credibility of the investment.

Illustration 2-2: Fraudster makes reference to major international agreements or programmes such as the Bretton Woods Agreements or the Marshall Plan to explain the overall scheme.

- Justify the inexplicable by resort to technical terminology;

Illustration 2-3: Funds in an account are said not be to at risk because they will be “scanned” by the trading bank, but not otherwise affected.

- Excuse a failure in promised performance;

Illustration 2-4: Government regulations, such as tax laws, or electronic funds transfer systems rules are referred to in explaining why the “trades” or payment is delayed, or why additional funds are required by the fraudster.

- Or build excessive reliance by the victim on the fraudster’s apparently superior knowledge.

Illustration 2-5: Fraudster rationalizes the disproportionate returns of the scheme based on an economic analysis that explains how banks purportedly increase the money supply.

- Misused technical terms may either exist and be used properly, may be used incorrectly or in an improper context, or may be entirely fictional.

Illustration 2-6: Actual terms such as “Factoring” or “Forfait” may be used incorrectly.

Illustration 2-7: Investment is said to involve trading in independent guarantees that do exist but are not “traded”.

Illustration 2-8: Investment is said to be made on a specific form, such as “ICC Form 1020”, but the form does not exist.

Illustration 2-9: Fraudster misuses or twists legitimate technical or scientific terms, such as a successful fraud in the oil and gas industry that referred to the fictional process of “sonic” fracturing to assist oil or gas recovery.

- Technical terms may also be misused in different ways:

- At different stages of the scheme;

Illustration 2-10: For example, they may be used to entice the investor, to obtain funds, to induce the transfer of control of assets, to explain why payments are delayed, or to prevent the investor from contacting authorities.

- Or beyond their intended purpose in order to validate a transaction.

Illustration 2-11: Commercial frauds often use technical terms regarding funds transfer to purportedly indicate the legitimacy of the transaction, but which are in fact only intended to indicate that a particular message was sent, but do not authenticate its contents.

**Advice:**

- Do not be intimidated or impressed by the use of technical terms and jargon.
- Insist on a clear explanation, regardless of the level of one's own knowledge or expertise.
- Understand all aspects of the transaction before investing.
- When performing due diligence, do not simply be satisfied with the existence of a specific technical term, such as "stand-by letters of credit", but ascertain whether the technical term or its role in the transaction is used properly in the context.
- Check into the existence and operation of any law under which taxes, fees and other sums are allegedly owed.
- Employees should be educated about commonly misused terms and phrases.
- The appropriate employee within an organization should be consulted on a specialized transaction, or should be part of the negotiating or document review team.

**See also:** Indicator 6 – Undue Secrecy; Indicator 8 – Frustration of Due Diligence; Addendum 1 – Performing Due Diligence.

**Indicator 3: Inconsistencies in the Transaction**

In attempting to mimic aspects of genuine transactions, commercial frauds often contain untrue or conflicting statements of material facts, omissions of material facts and other serious inconsistencies.

**Explanation:**

Commercial transactions operate under rule-based systems; multiple aspects, documents, details, and representations are consistent with one another and, taken as a whole, reflect the scope and purpose of the transaction. Any inconsistency or repeated inconsistencies that do not result from an agreed change in the transaction are removed in the case of legitimate commercial transactions. Transaction participants understand the representations and details and ensure that all aspects of the entire context of the transaction are consistent. On this basis they may with confidence accept transactional and contractual obligations.

In a sophisticated fraud, inconsistencies may not be obvious, such as in the case of frauds where professionals within seemingly reputable firms of lawyers, accountants and bankers may have been successfully misled by a fraudster, and have unwittingly assisted in creating fraudulent documentation. However, in a typical scheme, fraudsters are unlikely to concern themselves with transactional realities in their quest to find a potential victim. In fact, fraudsters may create inconsistencies intentionally, with the expectation that the more informed persons will walk away,



leaving only those potential victims who are most vulnerable. Further, fraudsters are not necessarily concerned that all aspects of the context of the transaction be consistent. They often use old, pattern frauds, developed by others decades ago, and simply adapt these old schemes to the Internet, or replace old names with invented modern sounding fictitious instruments, such as “Anti-Terrorism/Drug Free Certificates” and may not know of the fraud’s internal inconsistencies. Fraudsters often are not experts in the fields of investment or business contemplated by their frauds and, lacking such expertise, they inadvertently may create inconsistencies in the transaction within individual documents or between documents, or there may be inconsistencies between what is written and what is said on various occasions.

#### **Instances and Examples:**

- The nature of goods changes depending on the document examined.

Illustration 3-1: At the outset, a transaction involves shipments of one commodity, but without any commercial explanation, the goods being sold are described as a different commodity in later documentation.

- What is written or said is devoid of logic or common sense.

Illustration 3-2: The goods described in the transaction, or a financial instrument described in the transaction, do not exist or are not commercially traded.

Illustration 3-3: An invoice reflects ocean carriage, but the transport document reflects rail or truck transport only.

Illustration 3-4: The first document refers to “ABC Corp” while later documents refer to “XYZ Corp”, or one company may guarantee the first document, while another guarantees the second document.

Illustration 3-5: Container or seal numbers listed on bills of lading or other transport documents are suspicious, or do not reflect the proper numbering and lettering systems.

- Individual orders are out of context with the overall transactional history.

Illustration 3-6: An unusual quantity of the same product is ordered with a demand for next-day delivery to be shipped to a mail-drop address.

#### **Advice:**

- Read documents critically, take detailed notes of any oral representations, and require any oral representations to be incorporated into the documents.
- Do not rely solely on the documents presented for due diligence.
- Ask questions about inconsistencies and do not accept facile answers or excuses. Suspicious or illogical explanations when inconsistencies are raised may signal fraud.

- The presence of inconsistencies is unusual; the unresolved presence of inconsistencies is highly unusual; and both may signal fraud.
- If a transaction or activity occurs that does not pass one's own "common sense" test, then that alone is a good enough basis to consider the matter suspicious and to pursue due diligence.

**See also:** Indicator 1 – Irregular Documents; Indicator 8 – Frustration of Due Diligence; Indicator 14 – Irrational or Illogical Aspects or Explanations; Indicator 21 – Frauds involving Goods and Services; Addendum 1 - Performing Due Diligence.

#### **Indicator 4: Misuse of Names**

The person promoting a fraudulent scheme often seeks to enhance personal credibility or that of the scheme by associating it with the names of persons or organizations known, or likely to be known, by the person or entity to which the scheme is presented.

#### **Explanation:**

Names, particularly of those who are reputable or influential in the field, are misused in several ways in commercial frauds. Similarly, the names, logos, trademarks, catch-phrases, and symbols of a company or other entity, can be used in the perpetration of a fraud. A fraudster may suggest that individuals known within the field have reviewed and approved of the purported transaction, thus suggesting to the victim credibility, validity and enforceability of the fraudulent scheme. A fraudster may introduce or promote a scheme by asserting a false or exaggerated relationship with a person or entity known to the victim or its advisors. A fraudster may give the name of a well-known person or entity as his or her own or suggest an association with it, or a fraudster may simply adopt the name of another person or entity to hide the fraudster's own identity.

#### **Instances and Examples:**

- The names used in connection with commercial fraud may be of:
  - Well-known persons or organizations;

Illustration 4-1: A fraudster claims to be a protégé of the head of a country's Central Bank or Ministry or similar body, who is alleged to have provided advice regarding the scheme, but whose role and/or identity is not revealed.

Illustration 4-2: The fraudster introduces the potential victim to an actual or purported relative of an eminent person, such as the prime minister or a president of a country, who is willing to vouch for the fraudster or his or her proposed transaction.

- Individuals with whom the potential victim or the victim's advisors are familiar;

Illustration 4-3: The fraudster claims that the potential victim's business partner or friend has participated in the transaction when, in fact, that person has not.

- Or well-known organizations and rules.

Illustration 4-4: Documentation provided by the fraudster mentions the United Nations, or the International Monetary Fund or the International Chamber of Commerce, but gives no explanation as to its relationship to the transaction. Other references may be to ICC Rules, UCP 500, or SWIFT when the nature of the transaction does not correspond with the rules cited, or, more generally, to the involvement or approval of other “federal” or “national” or international banking or other authorities.

- A commercial fraud may be signalled where:

- The promoter of the transaction gives instructions concerning individuals or entities that the potential victim may wish to contact to verify the authenticity of the transaction:

Illustration 4-5: The fraudster suggests that an international or governmental entity approves of transactions of the type promoted. However, the fraudster warns the potential victim that if he or she contacts that body to ask about the transaction, the entity will be forced to deny the legitimacy of the transaction.

Illustration 4-6: The fraudster suggests that the president of a major bank has approved of the fraudster’s transaction and suggests that the potential victim contact the president to discuss the transaction, even providing the president’s telephone number and email address. However, the potential victim’s inquiries are in fact answered by the fraudster or a co-conspirator, who assures the potential victim of the legitimacy of the transaction.

- The potential victim cannot verify that the references made by the fraudster actually support the transaction:

Illustration 4-7: The fraudster states that a well-known celebrity or sports figure has invested in the fraudster’s purported transaction. Because the victim cannot contact the celebrity directly to discuss financial transactions, the reference cannot be verified.

- Or telephone numbers given to verify information are mobile telephone numbers, or do not correspond geographically with the address given.

#### **Advice:**

- An independent investigation of claims of affiliation should be conducted. Most well-known organizations have public information against which claims and documents can be compared for substantiation. However, note that elaborate schemes may involve the creation of false websites that mirror the authentic website of an organization, which may provide false information about the scheme.
- A solid investment opportunity should stand on its own merits and not rely on purported associations with well-known persons or entities.

- Do not rely upon or make assumptions about the use of names and reputations of alleged backers or prior investors without further inquiry and investigation.
- In countries or situations where it is difficult to investigate secret personal relationships with powerful people and organizations, extreme caution should be used by a prospective investor.
- Do not rely on a business card as a means of identification of the individuals with whom one is dealing.
- Professional intermediaries must also be aware of the dangers of relying on the use of names without an independent investigation.
- Organizations should actively and publicly defend their name and expose any improper use of it and should make publicly clear the organization's legitimate functions.

**See also:** Indicator 1 – Irregular Documents; Indicator 6 – Undue Secrecy; Indicator 8 – Frustration of Due Diligence; Indicator 10 – Ensnarement and Psychological Inducements; Indicator 15 – Fraud Based on Abuse of Personal Affinity or Relationships; Indicator 17 – Unusual Involvement or Participation of Professionals; Addendum 1 – Performing Due Diligence.

#### **Indicator 5: Disproportionate Returns**

Commercial frauds often guarantee high yields with little or no risk.

#### **Explanation:**

Every investor wishes to maximize returns. However, it must be remembered that returns are always proportionate to the perceived risk, which varies amongst investments. When the risk is high, investors require higher returns than they would receive from less risky investments before placing their capital at risk. Therefore, the higher the risk, the greater the promised return. Commercial frauds distort this principle of proportionality, promising high returns for little or no risk in order to induce investments. Often promised returns are even far in excess of what could be earned from highly speculative investments. The risk-free character of the proposed investment is emphasized using a variety of means, including promises or guarantees from the fraudster or from third parties or entities. Some fraudulent schemes purport to provide evidence that the returns are being earned or they may even actually pay such returns from the money originally invested or from money invested by other investors.

#### **Instances and Examples:**

- Commercial frauds promise:
  - Low risk;

Illustration 5-1: The literature in support of the investment provides assurances that the principal or principal and earnings are “risk free” or “without risk”.

Illustration 5-2: The funds are said to be in an account that is under the control of the investor and that the funds will not be moved without the investor's permission.

Illustration 5-3: The funds are said to be placed in an escrow account of a professional such as an attorney, which is intended to provide added confidence as to the safety of the investment and the funds. However, the professional may be deliberately assisting in the fraud or may be under the instruction of the fraudster rather than of the person depositing the funds.

Illustration 5-4: Phrases such as "riskless principal" are used out of context.

- Guarantees are made or given;

Illustration 5-5: The fraudster provides a personal guarantee or one from an accomplice, but such a guarantee is worthless.

Illustration 5-6: The fraudster promises a guarantee from a major bank or financial institution which will be provided when the investment is made.

Illustration 5-7: The fraudster indicates that the funds or investment are insured.

Illustration 5-8: The fraudster asserts that the funds are guaranteed by a governmental or international agency or organization.

- Or disproportionately high returns.

Illustration 5-9: The returns promised frequently range from 20 per cent per month to 50 per cent per month in a low inflation currency.

- The disproportionately high returns are explained in a variety of ways.

Illustration 5-10: High returns are justified by the volume of "trading" in which small profits per trade are accumulated. Usually the mathematics supporting these figures is flawed: the calculation may fail to take into account expenses, or may suggest more trades than typically take place in the given investment.

Illustration 5-11: Sales and market data are often manipulated, especially with respect to the time frame, to make it seem that returns are very high over a very short period of time.

- Note: Even the actual payment of promised high returns does not ensure the legitimacy of the investment.

Illustration 5-12: Alleged returns may be paid from the investor's own money or that of other investors and not from any real return on the investment.

Illustration 5-13: Such high returns often appear only as bookkeeping entries and investors are encouraged to "reinvest" by the promise of even higher returns.

**Advice:**

- If an investment scheme sounds too good to be true, it probably is not genuine.
- Perform due diligence by understanding the nature of the investment, its likely and possible risks and returns or consulting with an independent person who may be relied upon to provide appropriate advice.
- Beware of confidence builders, i.e. small, insignificant transactions which appear effective and offer suitable returns aimed at inducing further and more substantial investment.
- Excessive emphasis by a promoter on rate of return, or that an investment is “no risk” or “low risk” or “high return”, with little or no discussion of the substance of the investment should be a cause for concern.
- The returns promised are completely out of proportion to the risk assumed and to prevailing market rates of returns.

**See also:** Indicator 8 – Frustration of Due Diligence; Indicator 9 – Corrupted Incentives; Indicator 13 – Questionable or Unknown Source of Repayment; Indicator 15 – Fraud Based on Abuse of Personal Affinity or Relationships; Indicator 20 – Pyramid and Multi-level Marketing Schemes; Addendum 1 - Performing Due Diligence.

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