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Indicators of Commercial Fraud (A/CN.9/624, A/CN.9/624/Add.1 and A/CN.9/624/Add.2)

Compilation of comments by Governments and international organizations

Addendum

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II. Compilation of comments

A. States

5. Peru

[Original: Spanish]
[7 March 2008]

Senior Public Prosecutor – North Lima Judicial District

1. There is a clear need for this project in the face of current crime trends. Social change has brought about new forms of crime or an increase in existing forms. In the modern information society, the new types of crime have become more sophisticated with increasing use of advances in technology. Commercial fraud is being refined by means of these new technological aids.

2. The materials relating to the indicators prepared by UNCITRAL are appropriate to their purpose of commercial fraud prevention. The presentation of each indicator in three parts is ideal, the first giving an explanation defining the term; the second setting out instances and examples, which provide useful clarification for understanding the various circumstances in which the commercial fraud indicator in question can arise; and the third offering advice on how to prevent that type of commercial fraud from being committed.

3. Our suggestion relates to Indicator 1 (Irregular documents), which, because of developments in technology, needs to take account of the growth of electronic commerce where transactions are completed online and the documents containing the related contracts are on a digital platform. Notaries specializing in digital media thus need to carry out checks before decisions are made online if the complexity of an operation so warrants. Also, when contracts are accepted electronically, digital signatures should be used but checks must be made by international companies to guarantee authenticity of the signatures. To conclude, documents do not exist on paper alone but can also be in digital format; the Commission should therefore expand this topic with regard to case examples and advice.

Fourth District Prosecutor's Office, Puno – Puno Judicial District

4. The illicit commercial activities that are taking place at the global level are a matter of concern to the United Nations as a supranational body, which is addressing this issue through UNCITRAL.

5. As previously noted, commercial activities are also a component of organized crime. They now affect countries throughout the world, with particular impact on their criminal justice systems. Specifically, they involve transnational business operations, which are using more sophisticated tools, such as modern means of communication and international trade networks.

6. These new crime types infringe individual and collective rights and are increasingly affecting State interests as a result of globalization, the free market in commercial transactions and Internet commerce, enabling certain individuals, by operating jointly, to obtain profits illicitly on a large scale, thereby augmenting their

wealth. The groups carrying out such unlawful operations can be categorized as follows in criminal law:

1. Crime syndicates, which commit non-conventional offences on an international level;
2. Criminal organizations, which usually operate within a specific country;
3. Gangs, in which individuals participate in the commission of unlawful acts, on a smaller scale, and are better known and tend to operate in the area of a specific town.

7. We personally believe that illicit commercial activities primarily involve the following specific areas:

- (a) Arms trafficking;
- (b) Customs trafficking;
- (c) Labour trafficking;
- (d) Laundering of money or assets;
- (e) Corruption of public officials;
- (f) Influence peddling;
- (g) Falsification of documents.

8. A factor common to these crime types is the use of international trade to obtain illicit profits, which rise in proportion to the corruption of legal practices and engagement in illegal dealings. There is thus a correlation between increased unlawful gains and levels of corruption in business relations.

9. In connection with combating this new form of organized crime, some legal systems already criminalize the substantive offences while others still do not. This is therefore a matter of concern to the United Nations and specifically to UNCITRAL.

10. The project is a good initiative but the institutions responsible for the detection and prevention of these types of crime need to be strengthened, specifically authorities such as the prosecution service and the police. Also, the internal organization of debates, discussions, round tables and other activities should be promoted in order to provide guidance for persons entrusted with investigations.

11. It is suggested that, with a view to enhancing lay readers' understanding of the project, a glossary could be included at the end.

Second District Prosecutor's Office, Arequipa – Arequipa Judicial District

12. This project analyses the detrimental economic impact of fraudulent practices on world trade, a development which our country has sadly not escaped. While the market is now intrinsically international and we are witnessing increased flows of information, capital, technology and trade, with interconnected economies, trading blocs and market liberalization and integration, this new economic and commercial situation calls for the implementation of new codes of conduct and the presence of effective institutions, notwithstanding their commitment to modernity and the structural changes being made to confront the challenges of the modern world,

which include smuggling and revenue fraud, among other fraudulent commercial practices.

13. It is extremely important for this project to be widely disseminated in the public and private sectors as an informative document, thus alerting those involved in commercial transactions to the indicators of possible commercial fraud, which would not only help to prevent them from becoming victims but would also raise awareness of the occurrence of such offences.

14. It should be pointed out with regard to whistleblower policies, which are understood as one of the best practices in the prevention of commercial fraud, that it is essential that such policies are adequately regulated with the possibility of obtaining information which will identify the whistleblower, since anonymity for whistleblowers could allow unscrupulous individuals acting with unlawful intent to cause time and money to be wasted on futile investigations or distract the authorities so that a commercial fraud passes undetected, with serious harm to the national or international economy.

15. Concerning Indicator 1 (Irregular documents), the types of document involved should be classified as (a) genuine; (b) fictitious: documents not used in legitimate commerce; (c) forged: documents purporting to be genuine and used in legitimate commerce; and (d) counterfeits: documents used in legitimate commerce.

16. Also, institutions representing the corporate sectors and public sector institutions could through joint action:

- Establish a databank (for products liable to be the object of fraudulent transactions) containing prices, qualities, origins, producers, patterns and trends, which can be consulted in order to check information useful in preventing and controlling customs fraud;
- Set up technical assistance programmes to help business associations establish and/or improve systems for controlling their commercial operations;
- Design information systems to identify trade flows connected with laundering of drug-trafficking proceeds.

Third District Prosecutor's Office, Arequipa

17. In the definition of commercial fraud, reference is made to its "serious economic dimension" as one of its characteristics. This gives rise to a misleading interpretation since it relates to the scale of the commercial fraud but not to the actual existence of fraud. Identifying commercial fraud in terms of its serious economic dimension focuses solely on large-scale losses involving considerable sums, whereas cases entailing minor sums nevertheless also constitute fraud.

18. The project would appear to be concerned with examining fraudulent practices that have a major economic impact. Strictly speaking, however, commercial fraud can occur whether the economic impact is major or minor. In any case, the title of the study (*Indicators of Commercial Fraud*) seems inconsistent with its purpose if it deals only with commercial fraud having a major impact.

19. It should be borne in mind in connection with whistleblower policies, which are understood as one of the best practices in the prevention of commercial fraud, that it is essential that such policies are regulated so that it is possible to obtain

information which will identify the whistleblower, since anonymity for whistleblowers could enable unscrupulous individuals to make fictitious or fraudulent reports for unlawful purposes, causing time and money to be wasted on futile investigations, or to distract the authorities so that a commercial fraud passes undetected, with serious harm to the national or international economy.

20. Also, through joint action on the part of institutions representing the corporate sectors and public sector institutions, technical assistance programmes should be set up to help business associations establish and improve systems for controlling their commercial operations and information systems should be designed to identify trade flows connected with laundering of drug-trafficking proceeds.

21. It is very important that this project be disseminated in the public and private sectors, thus alerting those involved in the commercial sphere to the indicators of possible commercial fraud and thereby preventing them from becoming victims of such offences.

Fifth District Prosecutor's Office, Arequipa

22. Commercial fraud is best combated through prevention, which, as affirmed by UNCITRAL, should be achieved through education and training. We therefore believe that there is a need for the private sector (banks) to be made aware so that, whenever there are indications of potential commercial fraud, the prosecution service is notified so that it may conduct appropriate investigations, given that commercial fraud represents a serious threat which may be on the rise. A confidential telephone service should accordingly be set up at the prosecution service so that reports of potential offences of this type can be formally dealt with in order to prevent commercial fraud from occurring.

23. Mechanisms should be put in place so that, following the conduct of external audits, the appropriate body can be informed of cases of possible commercial fraud in order that it may undertake the necessary investigations.

Sixth District Prosecutor's Office, Arequipa

24. In the light of the document sent to this office and the information on indicators of procedural fraud provided by the State Prosecutor's Office, it may be stated that, with revision of the contents and introductory section, this could be a useful project in the prevention of international offences of this type, which also directly and indirectly affect our country, especially in the current globalization process.

25. As can also be seen from the UNCITRAL Commercial Fraud Project, some offences are connected with an organized corruption system operating at the international level and involving international criminal organizations that take advantage of a series of operations in order to commit offences of this type to the detriment of national economies, including our own. Such crimes are currently taking place but a lack of widely disseminated information on them makes combating them impossible. I therefore feel that this project, with the indicators set out in it, is a necessary document for detecting and preventing commercial fraud.

Seventh District Prosecutor's Office, Arequipa

26. Commercial fraud is the breach of legislative or regulatory provisions which the authorities are responsible for enforcing. It is committed for the purpose of:

- Evading or attempting to evade payment of customs duties, levies or charges on goods;
- Circumventing or attempting to circumvent prohibitions or restrictions applied to goods;
- Illegitimately obtaining or attempting to obtain grants, rebates or other refunds;
- Acquiring or attempting to acquire any illicit commercial advantage in contravention of the principles and practices of lawful commercial competition.

27. Commercial customs fraud includes all types of commercial fraud in breach of customs laws or regulations.

28. Commercial fraud is perpetrated primarily for financial gain and is committed where potential profits are greatest (for example, when high import customs duties are levied). However, commercial fraud is not confined to evasion of payment of customs duties but can also involve circumvention of prohibitions or restrictions on, for example, the transport of animals, military equipment, toxic products, etc.

29. As stated, one of the main motives for commercial fraud is financial gain. Personal rivalry and negligence are contributory factors.

30. There are various negative effects of fraud, which justify the fight against it. These are:

- Loss of State revenue;
- Adverse consequences for industry;
- Market disruption;
- Unfair competition;
- Social repercussions; and
- Risks for the consumer.

Main methods of fraud

31. Smuggling: a practice involving the import or export of goods in breach of laws and regulations or prohibitions in order specifically to evade or attempt to evade levies or charges through non completion of customs declarations or to avoid controls.

32. False description of goods: a technique used for the purpose of qualifying for reduced or nil duty rates or circumventing prohibitions or restrictions.

33. Overvaluation or undervaluation: the fraudulent misstatement of the value of imported or exported goods.

34. False origin: a scheme employed in order to take unwarranted advantage of preferential regimes applying to certain products and tariff quotas.

35. Abuse of inward or outward processing or temporary admission regimes: a technique used for the purpose of taking unwarranted advantage of exemptions or rebates provided for under such regimes; examples:

- No re-export or re-import of goods;
- Substitution of goods.

36. Abuse of import or export licence regulations: a practice whose aim is the avoidance of controls relating to the granting of licences, for example:

- Prohibitions or restrictions on imports or exports.

37. Abuse of transit rules: a practice involving diversion to domestic consumption. The following methods are used:

- False customs declarations;
- Fictitious transit of goods;
- Substitution of goods.

38. False statement of quality or quantity in order to take advantage of duty rates; examples:

- Declaration of a smaller quantity;
- Transport of goods hazardous to health;
- Mislabelling of goods (as to origin or composition).

39. Abuse of special arrangements.

40. Counterfeit or pirated goods:

- Counterfeiting: unauthorized use of a registered trademark on a product or on its packaging in breach of the rights of the trademark owner;
- Piracy: unauthorized reproduction of an article in breach of copyright.

41. The black market: the practice whereby transactions are not entered in a company's records in order to conceal illicit activities such as smuggling or undervaluation.

42. Registration of fictitious companies in order to benefit from unwarranted tax deductions.

43. Fraudulent bankruptcy: organized liquidation of companies which operate for short periods, running up tax or customs debts, and are then liquidated to avoid payment.

The main types of fraud

44. There are various types of commercial customs fraud, such as the misrepresentation of goods or of their end use in order to qualify for reduced or nil duty rates or to circumvent the fact that goods are prohibited or subject to restrictions. For such purposes, false descriptions are made on invoices or falsified permits are presented. We will deal here primarily with commercial fraud connected with false origin and false valuation of goods.

False origin

45. We will first examine the motives for false declaration of the origin of goods and then consider the methods of origin fraud.

46. Motives: There are special commercial agreements with other countries allowing goods to be freely traded. Importers try to ensure that duty rates are low or virtually nil for goods imported from developing countries by:

- Circumventing restrictions on exchanges between certain countries, for example trade embargoes (weapons);
- Circumventing quotas or import licence regulations on goods, such as textiles, agricultural products or toys, imported from certain countries;
- Circumventing anti-dumping duties levied on goods from certain countries.

47. How origin fraud is committed:

- The country of origin may be misstated on customs documentation (customs declarations);
- Counterfeit documents may be presented as proof of an advantageous place of origin; example: documentary evidence has to be provided of composition, processing and manufacture since these particulars are used to claim that goods are produced by a certain exporting country in order to benefit from preferential treatment.

False valuation

48. This takes the form of either overvaluation or undervaluation.

49. Undervaluation: The main aim of undervaluation of goods is to evade payment of duties through fraudulent misstatement of values declared to customs or through undeclared or undervalued payments made to or for account of the vendor.

50. The following are some examples:

- No statement of costs of transport to the place of direct delivery of the goods;
- Non-declaration of inputs (moulds, dies, etc.) used in the manufacture of the goods;
- Non-declaration of royalty payments or duties;
- No indication of deductions for goods returned to the exporter;
- Non-declaration of sales commission transferred in the name of the vendor;
- Non-declaration of payments connected with export quotas;
- False valuation of discounts granted;
- Misrepresentation of the relationship between importing and exporting companies (a subsidiary cannot be an independent company).

51. Overvaluation: While overvaluing goods for customs reasons may seem illogical, national customs services are increasingly affected by this type of fraud.

52. Motives:

- Overvaluation is used to circumvent anti-dumping duties levied on certain imports. The goods can then be sold at prices lower than those indicated in the declaration documents. As the resale value entails lower profits, the company makes higher gains in terms of direct taxation;
- Overvaluation can be used to circumvent foreign-exchange controls;
- Overvaluation can be used in the laundering of illicitly obtained money, which can then be invested abroad;
- Finally, overvaluation can affect a country's domestic market through the mass import of poor-quality products and goods of unknown origin.

Fraudulent documents

53. Double invoicing: This technique involves an illicit agreement between the exporter or broker and the importer. Two versions of the invoice are prepared: one stating a lower value for customs use and another showing the real price, which is sent directly to the importer. It is a common undervaluation practice. Sometimes there are two other sets of invoices in addition to those sent to the importer: one for the customs office of the exporting country and the other for the customs office of the importing country. In this case, if the customs agent works for the same company operating in both countries, there has to be complicity.

54. Fraudulent or incomplete invoices: This practice occurs when particulars relating to the customs value are misstated or not stated at all; examples:

- Reductions for defective goods;
- Non-declaration of inputs supplied to the vendor (for instance, if fabrics are sent abroad to be made into garments but the invoice subsequently mentions only the labour costs);
- Non-declaration of royalty payments or duties relating to the use of a trademark;
- Non-declaration of insurance costs.

55. Other fraudulent documents:

- International consignment notes (showing lower transport costs);
- Air waybills and bills of lading;
- Certificates of origin;
- Documents bearing false seals;
- Documents containing false descriptions of goods or of their end use in order to take advantage of lower duty rates or exemptions from duty or to circumvent prohibitions or restrictions.

Eighth District Prosecutor's Office, Arequipa

56. Suggestions regarding additional indicators:

- Fraud involving collusion between the fraudster and an employee of the defrauded enterprise (private company, State agency, etc.);

- Duration of procedures (business dealings, etc.): If a procedure is expected in advance to take a certain amount of time (for instance, six months), the swift conclusion of the operation may be an indicator of fraud; conversely, if an operation ought to be finalized quickly, a delay in its completion could be an indicator of fraud;
- In tendering processes: unscheduled changes to the timetable, little advertising of the bid, lack of precise information concerning the tendering conditions and referral to a specific individual with whom a personal interview has to be held in order to obtain full information;
- Irrational changes to the course of procedures: If a commercial, judicial or administrative procedure has to be carried out according to certain steps, any alteration to that process for irrational reasons, such as the inclusion of an extra step or a reduction in the number of steps, may be an indicator of fraud;
- Unexpected changes in staff responsible for commercial operations once the process has begun, especially when those excluded enjoy a good reputation. For example, a large company wishes to supply the State (Ministry of Health) with a certain product. Its bidder bribes the Minister in order to win the offer, whereupon the Minister, knowing the moral standing of the person in charge of the selection process, unjustifiably replaces that person with someone in his confidence. The replacement agrees to select the fraudster's company as the new supplier although the terms offered by it are not the most advantageous to the State. This example could also apply to any private company.

57. In the definition of commercial fraud, reference is made to its "serious economic dimension" as one of its characteristics. This would appear to be at variance with the facts and gives rise to a misleading interpretation since it relates to the scale of the fraud but not to the actual existence of fraud. Identifying commercial fraud in terms of its serious economic dimension focuses solely on large-scale losses involving considerable sums, whereas cases entailing minor losses nevertheless also constitute fraud even though they involve small sums. The project appears to be concerned with examining fraudulent practices that have a major economic impact. However, in the strict sense, the occurrence of commercial fraud is unrelated to the extent of its impact. In any case, the title of the study, *Indicators of Commercial Fraud*, seems inconsistent with its purpose if it deals only with commercial fraud having a major impact.

Tenth District Prosecutor's Office, Arequipa

Comments

58. While the globalization of relationships, in particular in the area of commerce, is becoming increasingly important worldwide since it brings benefits that are primarily economic for countries trading with each other, it has also given rise to the emergence of or an increase in criminal offences at the international level, such as commercial fraud, money-laundering or trafficking in persons, thus undermining intercountry relations and engendering mistrust.

59. Commercial fraud, as defined by the United Nations, is similar to the offence of obtaining by deceit, false pretences or fraudulent misrepresentation, committed against legal persons, as established by our criminal code, and is thus a property crime.

60. Because of the treaties being concluded by it, one of which (the free trade agreement) is still under discussion, our country must also begin to take account of the possible fraud or deception of which it could be the victim or instigator. In the latter case, we might lose trustworthiness in international dealings and be barred from agreements or treaties. As victims of fraud, businesses or the State could sustain countless economic losses, with detrimental repercussions for workers, since fraud can lead to bankruptcy or closure of companies and hence to unemployment.

61. The United Nations accordingly attaches importance to the issue of fraud and to alerting States to the need to take precautions and prevent unlawful acts of this kind, which are now being committed.

Suggestions

62. Given the incidence and international nature of these offences, we believe that they should be so classified in the criminal code as separate from other types of property crime since, because of their legal definition, other offences such as breach of trust are implicit in their scope.

63. Also, prosecuting authorities should be instructed in these matters so that they can identify such offences promptly and thus become more familiar with this crime type, its forms and connections, and with the evidence to be obtained during investigations.

6. Venezuela (Bolivarian Republic of)

[Original: Spanish]

[14 February 2008]

64. The Bolivarian Republic of Venezuela has no objections concerning the draft Indicators of Commercial Fraud prepared by UNCITRAL and wishes to state that they do not contravene current Venezuelan law.
