



Economic and Social Council

Distr.: General
31 January 2007

Original: English

Commission on Crime Prevention and Criminal Justice

Sixteenth session

Vienna, 23-27 April 2007

Item 4 of the provisional agenda*

World crime trends and responses: integration and coordination of efforts by the United Nations Office on Drugs and Crime and by Member States in the field of crime prevention and criminal justice

Results of the second meeting of the Intergovernmental Expert Group to Prepare a Study on Fraud and the Criminal Misuse and Falsification of Identity

Report of the Secretary-General

Addendum

Economic fraud

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* E/CN.15/2007/1.



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I. Commercial context of economic fraud

A. Commercial law

1. Most States provided information about laws regulating commercial activities, which range from the highly regulated to the largely unregulated. Most States have contract law or law of obligations based on the freedom to contract and circumscribed by additional rules intended to provide protection in situations of inequality, dishonesty or inadequate disclosure. Some also have more general consumer protections such as limits on advertising and standards for the quality of goods or services. Rules appeared to be designed to increase the stability and predictability of commercial dealings and to protect vulnerable parties. Many States had specific rules for specific types of commerce, and some had established specific agencies to administer these. Some also reported legislative or regulatory powers governing technical aspects of commerce, such as elements of the infrastructure of electronic commerce contracts¹ and identification.² A number of States also mentioned the possibility of civil lawsuits as a means of recovery, either as an exclusively civil option, or as a hybrid option in which civil claims could be based on a criminal conviction, and some mentioned other civil remedies, such as the voiding of contracts. Many also have additional requirements for commercial areas seen as vulnerable to fraud, such as corporate governance and breach of trust issues and areas such as telephone or Internet sales. One State observed that everyday commercial practice might not necessarily correspond with legislative ideals, noting that even where equality of bargaining power might be enacted in law, this did not necessarily mean that it would exist in practice.

B. Commercial technologies

2. Generally, the experts considered commercial technologies to include technological systems that had been developed or adapted or were commonly used to support elements of commerce. These could also be broken down into mass consumer technologies and other commercial technologies used by banks and financial institutions for smaller numbers of larger transactions. Many commercial technologies depend on the availability of supporting information and communication technologies. There appear to be differences in the availability and use of technologies within countries. A number of States reported greater access to and use of technologies in urban areas than in rural ones, and this was more pronounced in developing countries. The use of information, communication and commercial technologies has expanded substantially in recent decades. Telephone access has increased from fewer than 100 million in 1950 to about 1 billion

¹ Regarding electronic commerce legislation, see Model Law on Electronic Commerce of the United Nations Commission on International Trade Law (General Assembly resolution 51/162, annex); both the Model Law and the accompanying *Guide to Enactment* appear in a United Nations publication (Sales No. E.99.V.4).

² Regarding electronic means of identification, see Model Law on Electronic Signatures of the United Nations Commission on International Trade Law, *Official Records of the General Assembly, Fifty-sixth Session, Supplement No. 17* and corrigendum (A/56/17 and Corr. 3), annex II, and *UNCITRAL Model Law on Electronic Signatures with Guide to Enactment 2001* (United Nations publication, Sales No. E.02.V.8).

in 2000.³ Mobile telephone use has also rapidly expanded, especially in developing countries. Internet access has gone from zero in 1969 to 395 million in 2006, and is expected to exceed 500 million before the end of the present decade.⁴ Use of consumer commercial technologies such as payment (debit and credit) cards varied widely. Generally, developing countries estimated relatively low usage, while the most technologically developed countries reported a range between approximately 25 and 50 per cent of transactions and a shift from cash to the use of cards and other electronic means of payment. Most developing countries have no data on commercial technologies and a number of countries reported that only the companies involved would have such data. Developing countries reported higher usage of barter, but one developed country also noted increases in barter supported by the Internet. The ways technologies are used are also expanding. Electronic commerce, in which technologies are used for the advertising and sale of goods and services as well as payment, is expanding in countries where it is technologically viable, but is still a small fraction of overall commerce.

II. National experiences of economic fraud and legislative responses

A. Meaning of economic fraud and scope and elements of fraud offences

3. In most States, the legislative definition of fraud is exclusively economic, but practical use of the term sometimes includes other forms of crime that involve elements such as dishonesty or deception, but not necessarily any economic element. Most of the legal definitions of fraud were considered criminal law and contained economic elements. Some States also reported elements of their commercial law that addressed fraud and related problems using non-criminal measures such as controls on advertising. These were seen as anti-fraud measures, but generally addressed a broader range of conduct not limited to criminal fraud. This is consistent with earlier work undertaken by the United Nations Commission on International Trade Law (UNCITRAL), which suggests that commercial concepts of fraud include some conduct that some States would not necessarily see as criminal (A/CN.9/540, paras. 12 ff.). Some States indicated that they considered fraud as including non-economic crime, but reported fraud offences based on economic losses, and non-economic offences, such as forgery or impersonation, which were not legally defined as “fraud”. Common-law definitions are based on the original English concepts of fraud or false pretences, which include economic elements, but are defined in case law, and some common law States reported statutory offences supported by non-statutory definitions.

4. There was a high degree of consistency in the elements of the fraud offences provided or described by States. The vast majority include some form of dishonesty or deception, some form of economic loss or transfer, and the need for a causal connection between the two. The economic element covered a wide range of

³ International Telecommunication Union, *World Telecommunication Development Report 2002: Reinventing Telecoms* (2002).

⁴ <http://www.isc.org/index.pl?/ops/ds/>.

financial or other material benefits or losses, including tangible property, financial or other interests, and less tangible losses such as exposure to risk or loss of expectation value, even if these did not materialize. The elements of dishonesty or deception were also consistently present. Some States required active conduct intended to mislead, while others also included deception through the withholding of information, failing to provide information or taking advantage of the fact that the victim did not have relevant information. One issue that has arisen in States where automated commercial forms of identification are used is whether a machine or system can be deceived, but most systems appear to have dealt with this issue in some way, treating machine-related variants as types of fraud. Similar issues arise with respect to cases where legal persons are deceived, and these too, are generally seen as forms of fraud. Some States appear to have offences only for individual transactions, while others also have offences of defrauding the public as a whole, perpetrating mass frauds or operating fraudulent schemes, which may simplify prosecution, evidentiary and jurisdictional issues in some cases.

5. Most fraud succeeds by imitating legitimate commerce, raising the need for commerce-based initiatives in response, and almost all States indicated that they dealt with fraud as both a commercial and a criminal matter. Laws regulating contracts, advertising and remedies for defective or misrepresented goods were reported, as were regulatory regimes establishing such elements as minimum standards for commercial practice, criminal or administrative prohibitions and offences, inspection powers and bodies empowered to monitor laws and practices, consider disputes and apply remedies. More specific provisions were directed at specific commerce such as stock markets, insurance or real property transfers, or key areas of professional practice such as law or accounting.

B. Approaches to classifying economic fraud

6. States were asked about the legal basis on which they classified fraud. The responses disclosed two strategies for criminalization, depending on whether fraud was classified in detail or not. Some States reported only a very small number of general fraud offences, while other States reported larger numbers of more narrowly framed, specific offences. Definitions based on *modus operandi*, types of infrastructure attacked or involved and victim status or characteristics were the most common. It was also clear that while national legislation sometimes followed the typology suggested by the questionnaire, the suggested categories overlapped. Descriptions such as “mass-market fraud”, “advance fee fraud” and “pyramid” or “Ponzi” fraud schemes are all used primarily as non-legislative terms, although several States did report specific offences or other legal provisions. Some States have criminalized frauds based on devices, passwords or access codes or the use of telephones or telecommunications, and several have adopted offences that criminalize preparatory steps, such as the theft of, possession of, or trafficking in computer passwords, credit card information or devices used to “skim” and copy the data from credit or debit cards. Many States reported fraud offences based on the attacking of public structures such as social benefits or tax systems, and private commercial structures such as insurance, credit card, banking or other financial operations. Fewer States reported fraud offences based on the type of victim or type of offender, but a number did consider these factors as the basis for aggravated

offences or sentences. Specific groups of potential victims accorded additional protection included the elderly, minors, the mentally disabled, legal persons and the estates of deceased persons. Some States also apply additional measures to those in positions of trust, such as lawyers, accountants or corporate officers, and in some countries these are further supported by regulatory and disciplinary requirements imposed by governing bodies for key professions.

C. Types of fraud encountered by States

7. States have encountered a wide range of different types of fraud and, even within individual States, no single typological framework exists for classifying it. A further complication is that many frauds are effectively hybrid or compound, using more than one medium or message for different stages of the fraud, and the same victims can be targeted more than once by offenders using different messages. All of this makes classification difficult, and approaches to classification in each State may differ depending on who does it and why. Different approaches apply to offences and other legislative provisions that must support legal proceedings, working classifications used by law enforcement and other investigators for practical and training purposes, and criminological classifications intended to support research and policy development. Further categories are added by private sector interests, often based on the commercial sector involved, such as all types of bank, insurance or credit card fraud, and in accordance with needs such as loss prevention, audit requirements and civil litigation to recover proceeds.

8. While there are some superficial variables attributable to differences in language, culture or commercial practice, the underlying problem of economic fraud appears to be fairly universal, described in similar terms by countries from different regions and at different levels of development. To a large extent, reported differences appear to relate more closely to difference in underlying commerce than any other situational factors. Frauds involving credit cards, real property, financial markets, and the counterfeiting of currency were widely reported, for example, whereas frauds involving subject matter such as mining and trading in valuable minerals and maritime frauds were reported only by States with substantial legitimate commerce in those areas.

9. The specific types of fraud raised by States included types defined by method, such as “advance fee” frauds, pyramid or “Ponzi” schemes, computer frauds and frauds using paper documents; frauds defined by the system or interests affected, including frauds relating to bankruptcy, loans, real estate transactions, charitable appeals, maritime transport, stock markets, insurance, or commercial frauds in general; mass frauds defined by the large numbers of victims; telemarketing and telecommunications frauds, in which telecommunications were either the medium used or the proceeds generated; the counterfeiting of goods or currency; and frauds against government or public interests, including immigration systems or documents, procurement systems, tax systems and public benefits systems. Some States had separate offences for cases where government or public interests are defrauded, while others relied on more general offences, in some cases linked to aggravated punishments. Corruption offences such as bribery are seen by some States as a form of fraud against government, and are also often encountered as an

element of larger fraud schemes, when officials are bribed to ensure the success of the primary fraud.

D. Types of fraud criminalized by States

10. States reported a wide range of specific offences of fraud and related or preparatory conduct. Many States have found it necessary to expand established offences or adopt new ones to deal with recent innovations by offenders, especially in the area of computer-related frauds. Computer fraud offences are foreseen by article 8 of the Convention on Cybercrime of the Council of Europe,⁵ and a number of States reported offences of computer fraud or more general computer-related crime offences that could apply in fraud cases. These included possession, trafficking in or use of instrumentalities for computer-related fraud and offences relating to computer hacking or the unauthorized access to or use of computer or telecommunication systems.

11. Other types of fraud that were the subject of specific offences included: frauds using specific types of documents, including testamentary instruments, real estate documents and financial instruments; frauds against specific types of commercial activity, including bankruptcy proceedings, insurance frauds, frauds involving financial markets; bank frauds and credit card frauds; frauds involving gambling or lottery schemes, and counterfeiting private intellectual property. Some States also have specific offences covering frauds against the State itself, which may include corruption offences, and the European Union requires its member States to criminalize frauds that affect the European Union's financial interests or funds covered by its budget.⁶ Other frauds against the State included frauds against public procurement systems or public benefits systems, military fraud offences, frauds in municipal codes, fraud offences in laws governing professions and trade unions, and frauds affecting political parties or similar organizations. Some forms of tax evasion and the counterfeiting of currency or stamps are also seen as types of fraud in some States. Smuggling offences may be treated in some States as frauds if the purpose is to avoid excise taxes on commodities that are legal in that State, such as tobacco, in addition to trafficking in illegal commodities such as narcotic drugs. A number of related or preparatory offences were also reported, including: identity-related crimes such as impersonation and misuse of identification documents or identity information; abuses related to documents other than identity documents; the falsification, destruction or tampering with electronic data; some corruption offences; arson and other forms of property damage in support of fraudulent insurance claims; and, depending on the fundamental principles of each State's domestic law, conduct such as organizing, directing, aiding or abetting, attempting and conspiracy to commit fraud.

⁵ Council of Europe, *European Treaty Series*, No. 185.

⁶ Convention, drawn up on the basis of Article K.3 of the Treaty on European Union, on the protection of the European Communities' financial interests, *Official Journal of the European Communities*, No. C 316, 27 November 1995, p. 49.

E. Punishments for economic fraud

12. Punishments generally reflected the fact that economic fraud is not a violent offence and that there is a very broad range of ways fraud can be committed and a broad range of degrees of harm it can cause. Cases ranged from single offences with relatively minor harm to a single victim, to major corporate or commercial frauds and mass frauds that have generated losses in the hundreds of millions of dollars, affected many victims, caused major bankruptcies, and in some cases proved serious enough to destabilize Governments or cause damage to national economies. Many States reported either a series of fraud offences of escalating seriousness or single offences with lists of aggravating factors that affected potential sentences that could be imposed by their courts. The most commonly cited factor was the size of the fraud in terms of the numbers of victims affected or proceeds generated. Other common aggravating factors included repeat-offending, mass frauds, breach of trust or other abuse of power or inequality between offenders and victims, the involvement of organized criminal groups or the commission of money-laundering offences, and frauds that targeted or affected government or public interests. As noted, underlying policies generally reflected the need for additional deterrence to protect particularly vulnerable victims such as the elderly or to deter persons in positions where fraud was seen as exceptionally likely or damaging, or to protect the integrity of key commercial systems or documents.

13. Almost all States either reported that some or all of their serious fraud offences fell within the meaning of “serious crime” in article 2, subparagraph (b) of the United Nations Convention against Transnational Organized Crime (General Assembly resolution 55/25, annex I),⁷ or provided descriptions of offences that appear to meet those requirements. Punishments that could be imposed ranged from 0-3 months for minor offences, up to maximums of 30 years for more serious cases, and one State mentioned that mandatory minimum punishments applied to some types of fraud. Most States also provided for fines or confiscation, both as a punishment for less serious cases and as a sanction for legal persons, especially where the legislative framework only extends full criminal liability to natural persons.⁸ Specific sentencing conditions are also imposed on a case-by-case basis in many systems. Non-criminal penalties such as loss of professional status or licences were also mentioned. Within the framework of legal sentencing powers, there is also the more practical question of how they are applied by the courts and the ability of prosecutors to produce evidence of the severity or seriousness of the impact of frauds. In sophisticated commercial frauds, the evidence may be complicated and difficult to understand, especially in legal systems where the trier of fact is a jury or magistrate. In mass fraud cases, large numbers of victims cannot all be called into court, and it is usually necessary to produce secondary or expert evidence of the true extent of harm and numbers of victims affected. In transnational fraud cases, it may

⁷ Note that article 11, paragraph 2, of the Convention requires, inter alia, that any discretionary legal powers be exercised to maximize the effectiveness of deterrence in respect of offences covered by the Convention, which would include serious frauds. The requirement in article 11, paragraph 1, to apply sanctions that take account of the gravity of the offence only applies to the offences actually established by the Convention and Protocols, however, and would not apply in fraud cases.

⁸ See also the Convention on the protection of the European Communities’ financial interests, article 4.

be difficult to have expert opinions or summaries admitted as evidence and some individual victims may not be able to travel. This problem may be addressed in some cases by mutual legal assistance in the form of video-link testimony under the Organized Crime Convention,⁹ where applicable.

F. Liability of legal persons

14. Criminal liability entails moral culpability, high standards of proof, elements of intent and relatively severe punishments, which in some legal systems can only be applied to natural persons. Most States indicated that they applied criminal liability to legal persons, and one extended it to both legally and factually established bodies. Several other States indicated that they did not extend criminal liability, but did provide for administrative liability and appropriate punishments. All of the States that had criminal or administrative liability provided for fines, and some included other measures, such as confiscation. Some also had specific judicial powers such as barring specified natural persons from involvement in a company and ordering that a legal person be supervised or refrain from certain specified business activities. Some States also mentioned civil liability, imposed not by the State but by the courts in response to a private action brought by another party. This was usually the victim, although some systems now allow the State to bring a civil action and some have made provision for the recovery of civil damages based on a criminal conviction.

III. Assessing the scope and extent of fraud

A. The reporting and recording of fraud

15. Reporting and recording problems make it difficult to obtain accurate data from original sources, and difficult to assess the degree of accuracy of such data as are obtained. There is widespread agreement among experts on fraud that it is systematically under-reported. Twenty-two of the 24 States that expressed an opinion or provided evidence on this question expressed a similar view, as does earlier work on the subject of commercial fraud undertaken by UNCITRAL (A/CN.9/540, para. 6 (c)). Some States noted that under-reporting could also produce distortions in information about the relative prevalence of specific types of fraud because some specific types may be affected by under-reporting to a greater or lesser degree than other types. In some States, the availability of multiple public and commercial entities to which frauds could be reported was a concern, as was the fact that data collected by commercial sources were not always available to those compiling criminal justice statistics or compatible with those statistics.

16. Many reasons were given for under-reporting and most were consistent among States. The most commonly cited reason was the fact that victims, including both natural and legal persons, are embarrassed or humiliated and seek to avoid the publicity inherent in criminal proceedings or what one State described as “reputational damage”. The perception by victims and others that victims are partly

⁹ See article 18 (mutual legal assistance), paragraph 18; see also the United Nations Convention against Corruption (General Assembly resolution 58/4, annex), article 46, paragraph 18.

responsible for their own misfortune has been identified as an impediment not only to reporting, but also to an effective response by law enforcement and society in general.¹⁰ Frauds deceive victims and often contain elements intended to persuade victims not to report, including the fear of self-incrimination or loss of proceeds, or by persuading them that they have made a bad commercial bargain and are not victims of a crime. Victims also often believe that claims will not be taken seriously, that the costs of recovery or prosecution would be greater than any benefits, or that reporting losses to their banks or credit card issuers is more likely to lead to recovery than reports to criminal justice agencies. Commercial entities that encounter fraud tend to rely more on their own internal investigative and other processes than criminal justice measures. Victims also see only their own individual case and may underestimate the seriousness of the crime or the importance of reporting, especially in some forms of mass fraud or commercial fraud.

17. To confirm the degree of under-reporting and estimate the true extent of the problem, it is necessary to compare reported rates of victimization with actual rates, usually obtained by extrapolating mass surveys of population samples. Only one State indicated that it had gathered such information, although several others indicated that they saw a need for it and that projects to obtain it were under consideration or being developed. Several States expressed concern about the quality of available data and indicated that measures were already under consideration to obtain a more accurate and complete picture. In the State that did report data, approximately 30 per cent of persons who told the mass survey that they had been victimized had also reported this to official sources, but 67 per cent had reported it to appropriate private sources, such as credit card issuers or banks. This supports the conclusion that only a small fraction of overall fraud is reported and that victims are more concerned with recovering their losses than with criminal justice measures.

B. The quantification of fraud

18. The counting of fraud cases can produce substantially different results depending on how cases are reported and recorded. Mass fraud schemes tend to produce large numbers of cases if occurrences are based on counting numbers of victims or complaints, but lower rates if numbers of offenders, fraud schemes or prosecutions are counted. A third picture may emerge if the amount of losses or proceeds of fraud are counted, because areas such as commercial fraud tend to involve small numbers of offences with very large losses, while mass-marketing frauds often involve very large numbers of smaller offences, but can still generate very substantial proceeds. Also, the quantification of losses to victims and of proceeds in the hands of offenders can provide different results. In simple frauds there is often a direct link between losses and proceeds, but in the case of some complex fraud schemes, corporate frauds and pyramid or "Ponzi" schemes, the indirect losses and non-monetary damages can far exceed any proceeds realized by offenders or recovered by authorities or victims. There are also substantial differences between information gathered by criminal justice systems for policy

¹⁰ Governments of Canada and the United States, *Report of the Canada-United States Working Group on Telemarketing Fraud* (November 1997), section 4.1, "Educating the general public".

purposes and by private businesses for commercial purposes, and commercial data may not be shared for business reasons.

C. Rates and trends in fraud

19. Most States did not provide concrete statistics on rates of fraud; of the 32 States that provided information, 26 reported either general increases in fraud or the belief that such increases existed. Four States reported stable rates, two reported declining rates and the remainder had no information or did not respond. This was consistent with the views of the experts, as well as earlier work by UNCITRAL on commercial fraud (A/58/17, para. 235, and A/CN.9/540, para. 5). A number of States expressed the view that there was a connection between overall increases, increases in transnational fraud and the expansion of access to information, communication and commercial technologies. Only five States provided statistical data. Of these, two found increases, one reported inconclusive data and one reported decreases, but noted that these might be attributable to changes in reporting or recording. One State reported very large increases, of up to 1,400 per cent in the seven-year period from 1999-2005, and another described “dramatic” increases in the use of information and communication technologies by offenders, both to defraud victims and to transfer and conceal proceeds. Information provided by States generally did not address the question of whether the substantive scope of fraud is increasing, but the examples provided and other evidence suggest that the range and diversity of offences has also expanded. Whether there is real expansion or not, the scope of fraud offences encountered by States and the commercial community is clearly very broad, reflecting the full diversity of legitimate commercial activity within and among the Member States.

20. Several critical questions arise for national and global statistical analysis. Under-reporting makes it difficult to assess real occurrence levels and may distort information about the relative prevalence of different types of fraud. Legal definitions vary, and the same fraud may be counted as one occurrence or many in different systems. Population trends may also have an effect: several States reported that commercial practices and access to and use of relevant technologies were more prevalent in urban areas than rural ones, for example, and others reported data suggesting that specific forms of fraud and criminal techniques may migrate from one place to another with offenders. Fraud imitates legitimate commerce, making variations of commercial practice likely to produce parallel variations in fraud over time, between countries or regions, and with respect to specific areas of commerce. Conditions such as post-conflict reconstruction and major economic development or transitions can also have a substantial impact on fraud, as the confusion between old and new economic principles and specific activities such as major reconstruction efforts and the privatization of State-owned operations provide opportunities for fraud offenders. Several States also noted that data reported were divided among criminal justice agencies, other agencies and private sector entities, raising a need to identify gaps and compensate for multiple reporting.