

ECONOMIC CRIME AND THE GLOBAL ECONOMY: UNDERSTANDING THE THREAT AND IDENTIFYING EFFECTIVE ENFORCEMENT STRATEGIES AND COUNTERMEASURES

*John D. Arterberry**

I. THE GLOBALIZATION OF ECONOMIC CRIME

“Laws stop at borders, but crime does not.”
Speaker at 1997 World Economic Forum,
Davos, Switzerland

During the 1990s, we have witnessed the emergence of the Global Economy from a largely theoretical concept, to a vital and growing force in the affairs of nations. Evidence of that growth can be found in the airline industry. According to a recent news report, passenger volume in international commercial flights soared from 26 billion passenger miles in 1960 to 3.5 trillion miles in 1990.

While the Global Economy has developed, we have experienced a corresponding globalization of crime. Whether engaged in traditional organized crime activities like narcotics trafficking or sophisticated economic crimes like the BCCI scandal, criminals and their crimes now show no respect for political boundaries or geographic barriers and exploit the jurisdictional complexities both to expand and to conceal their crimes.

Increasingly, experts and leading law enforcement officials are sounding warnings about the threats posed by the globalization of crime. Economic crime stands at the forefront of this new wave of lawlessness that threatens the stability

and prosperity of global commerce. Those of us in law enforcement face an urgent challenge: effectively countering this global crime wave by overcoming barriers presented by institutional rigidity and national political considerations.

A. Defining the Threat

Often termed “white collar” or “financial” crime, economic crime inflicts its harms in many ways. Most directly, there are the financial losses suffered by fraud victims. Other harms are less apparent. At a meeting of police officials from 23 countries in September, attendees were told that the investment by criminals of their illicit funds in the world economy is generating annual profits of some \$500 billion, about 2% of the global financial activity. These funds may not only corrupt otherwise legitimate enterprises through which they flow, but also provide seed money for new and more damaging frauds.

1. A Menu of Economic Crimes

Economic or white collar crime presents itself in many forms. The crimes range from investment frauds that target the life savings of senior citizens to sophisticated bank frauds that use computers to divert bank funds to hidden accounts. No matter the degree of sophistication, there will always be common elements in the crime: lying, cheating or stealing will be at the heart of the scheme.

* Deputy Chief, Fraud Section, Criminal Division,
United States Department of Justice, U.S.A.

(i) *Financial Institution Fraud*

During the 1980s and 1990s, financial institution fraud has been a prominent and persistent problem. In the United States, we experienced a crisis in our savings and loan industry that resulted, in part, from pervasive fraud and other abuses requiring a massive government response. To date, the federal government has suffered losses in excess of \$200 billion resulting from the savings and loans (S&L) debacle.

Although the S&L crisis is behind us, financial institution fraud continues to be an economic crime priority for the federal government. Mortgage fraud inflicts losses estimated at \$60 billion each year. Cheque fraud involving counterfeit cheques is conducted by organized rings that range across the United States and cause losses to banks of about \$6 billion yearly.

On a more global dimension, the BCCI scandal demonstrated the vulnerabilities in regulation of multinational financial instruction. It also demonstrated the benefits obtained through international cooperation. Even though its citizens were not victimized, the United States successfully prosecuted BCCI for defrauding its banking regulators. Through that prosecution the United States has forfeited more than \$1 billion of BCCI-controlled assets, an action that has enabled the world community to compensate many of the individual depositor victims.

(ii) *Insurance Fraud*

Insurance fraud schemes may victimize either the insurer or the insured. Many schemes seek to tap the immense reservoir of assets held

by legitimate insurance companies. Arson for profit, staged accidents creating sham-injury and property damage claims, and inflated automobile body repair bills are examples of schemes aimed at the insurance companies.

Alternatively, insurance businesses may simply be a clever facade for massive fraud schemes. Unscrupulous promoters will establish insurance operations using "rented" or fraudulently inflated assets to satisfy government-established capitalization and reserve requirements. These operations often use off-shore shell entities to facilitate and conceal their frauds. The perpetrators collect policy payments from unsuspecting individuals and businesses before abruptly ceasing operations and departing with the scheme proceeds.

(iii) *Government Program Fraud*

Government programs and operations also are vulnerable to fraud. Dishonest claimants in government social welfare programs undermine citizen support for this effort and cause losses to the taxpayers of billions of dollars each year.

Health care presents a dramatic example of this problem. In the United States, health care has government programs and private sector components that are equally susceptible to fraud. In addition to individual, corporate and private insurance expenditures for health care, the federal government provides various health care programs that entail federal outlays of hundreds of billions of dollars annually.

110TH INTERNATIONAL TRAINING COURSE
VISITING EXPERTS' PAPERS

Some estimates place spending on health care in the United States at more than \$1 trillion each year, and as much as 10 percent of that amount, or about \$100 billion, resulting from fraud and related abuses. With such enormous sums of money spent each year, it is not surprising that frauds have proliferated. Health care fraud in the United States thus has emerged as one of the most serious domestic crimes in this decade.

The Department of Justice has instituted an aggressive enforcement campaign against health care fraud. Convictions in health care fraud cases have increased over 300 percent since Fiscal Year 1992 and hundreds of millions of dollars have been returned to the federal treasury through these prosecutions and related civil cases.

(iv) *Commercial Bribery and Foreign Corrupt Practices*

In the private sector, one of the most corrosive and costly abuses is commercial bribery. Businesses are victimized by dishonest employees who, in exchange for bribes, cause their companies to purchase defective goods, enter into inflated or bogus contracts or otherwise cheat their employers.

Closely related to commercial bribery is bribery of foreign officials by corporations seeking to obtain or retain business in foreign countries. In the United States, the Foreign Corrupt Practices Act expressly prohibits such conduct. Efforts are underway to obtain international agreement on similar prohibitions.

(v) *Credit Card Fraud*

Nothing symbolizes the global economy in personal terms better

than the credit card. Accepted universally, the credit card has revolutionized commerce and transformed business and personal travel. The credit card industry tallies billions of dollars in worldwide commerce annually. On the negative side, the industry suffers billions of dollars in fraud losses each year. Visa alone acknowledged in 1997 annual worldwide fraud losses at well over \$700 million.

Closely akin to credit card frauds are schemes in which victims' identification is appropriated by criminals and used to obtain funds and property through credit cards and bank accounts. Approximately 25 percent of credit card losses in the United States can be traced to this relatively new crime known as "identity theft". Identity thieves obtain, through various fraudulent means, the personal identifying data of their victims, including names, addresses, telephone numbers and federal Social Security numbers, which they then employ to gain unauthorized access to bank and credit card accounts. A consumer magazine reports that more than 1000 cases of identity theft occur each day in the United States. Just this year, federal law was amended to address this abuse.

(vi) *Securities / Investment Fraud*

Investment and securities fraud blossomed during the boom years of the world's equities markets in the late 1990s. The mutual fund industry in the United States, with assets of about \$5 trillion, is now larger than the nation's banking industry.

The euphoria created by enormous gains in the market prices of

securities has led investors to discard caution and place their hard-earned funds, often representing their retirement savings, to promoters who promise unrealistic profits to their victims. The securities industry estimates about \$6 billion annually in investor losses to securities fraud in the United States.

2. Costs of Economic Crime

Beyond the direct losses inflicted by fraud, which total in the tens of billions of dollars each year, there are less apparent costs. For example, businesses incur substantial expenses stemming from efforts to prevent and detect fraud. These precautions include comprehensive audits, large security staff, and sophisticated monitoring and other high-tech preventive measures. An official of a private security firm stated, in remarks at an international conference, that there has been an explosion in the private security industry, which currently employs 1.6 million individuals and consumes \$65 billion in resources. The speaker estimated that by the turn of the century the industry will grow to \$100 billion and employ 2 million persons. Ultimately, these costs are passed on to the consumer or are absorbed by businesses as profit reducing expenses.

Fraud also exacts less tangible losses. It distorts the flow of commerce and disrupts the development of global trade. Its staggering costs stifle developing economies and can undermine the stability of banks and other commercial enterprises. Economic crime, simply stated, is one of the greatest threats to the realization of a vibrant and healthy global economy.

II. COMBATING ECONOMIC CRIME: STRATEGIES AND COUNTERMEASURES FOR AN EFFECTIVE GLOBAL RESPONSE

A. Criminal Enforcement Measures

Success in fighting white collar crime requires a focused and coordinated response that blends the domestic effort with the broader international response. On the domestic front, available resources must be applied to the most pressing economic crime problems. These priorities can be set through a consultative process that includes the investigative and prosecutive authorities, as well as all relevant government departments and agencies.

International cooperation and mutual legal assistance treaties and agreements are essential tools in fighting global economic crime. As countries focus their attention on transnational crime, the need to modernize the methods by which we obtain legal assistance from other sovereigns becomes more apparent.

1. Domestic Strategies

(i) *Investigative Techniques*

During the past two decades, the Department of Justice has formulated varied approaches in investigating and prosecuting economic crime. We have moved away from the traditional practice of strictly separating investigators and prosecutors. Instead of keeping the prosecutor away from the investigative process, we regularly team agents and prosecutors to investigate cases jointly. This encourages closer collaboration and consultation in developing an investigative plan and leads to more expeditious completion of that phase in the development of a criminal case. At the same time, this collaboration

110TH INTERNATIONAL TRAINING COURSE
VISITING EXPERTS' PAPERS

ensures that promising avenues of investigation are not overlooked, that successful strategies for prosecution are fully exploited and that legal pitfalls are avoided.

Undercover operations (UCOs), originally developed as a means of infiltrating traditional organized crime groups like the Mafia, are now an important part of our arsenal of anti-fraud weapons. UCOs are especially valuable in exposing corrupt firms and individuals imbedded in regulated sectors of the economy. UCOs provide additional deterrence by keeping the criminal element off balance. White collar criminals can never be certain that the apparent collaborator may not actually be an undercover agent ready to expose their criminal activity.

(ii) *Prosecutive Strategies*

Prosecuting economic crimes presents many challenges. The schemes are often complex and potentially confusing. Thus, presenting the evidence necessary to prove criminal conduct may require numerous witnesses and voluminous documentary exhibits.

Experience gained by federal prosecutors over the past decade suggests that there are certain strategies that significantly enhance prospects for success. For example, charging decisions can sharpen the theory of prosecution and reduce some of the evidentiary burdens inherent in these cases. Rather than focusing charges on the entire episode of criminal conduct, our experience has shown that selecting the most egregious acts or those transactions for which the evidence is strongest

not only reduces the burden of preparation and presentation for the prosecutor but also facilitates a better understanding of the case and the evidence by the adjudicatory body.

Prosecutors and investigators may be grouped together in specialized units, or task forces, to concentrate on a particular economic crime problem. Task forces proved especially effective in addressing the frauds uncovered during the savings and loans (S&L) crisis in the United States earlier in this decade.

Denying criminals the fruits of their crimes through the forfeiture of their assets is one of the most dramatic and effective economic crime prosecutive tools to gain prominence during the 1990s. Forfeiture eliminates the profit in crime and also serves to remove valuable instrumentalities of crime, whether aircraft, office buildings or the criminals themselves.

At the end of 1997, approximately \$450 million had been deposited into the Department of Justice Asset Forfeiture Fund. The funds are shared with state and local law enforcement agencies to supplement their crime-fighting assets. In addition, the fund assists in compensating crime victims.

2. International Strategies

Established and predictable mechanisms for obtaining evidence from foreign jurisdictions is essential to fighting economic crime on the international front. Mutual legal assistance treaties (MLATs) are one of the most common means of achieving this goal. Rather than relying on the cumbersome process of letters rogatory, which invokes time-consuming

diplomatic processes for conveying assistance requests, nations are turning increasingly to the MLAT to ensure that borders are not barriers to pursuing economic criminals.

Treaties for extraditing individuals charged with economic crimes are being renegotiated in order to incorporate, as covered crimes, more modern versions of fraud and related offenses that may not have existed in domestic law when the treaties were first executed.

(i) *Regulation*

A key component in combating economic crime is effective regulation. Regulation helps by suppressing practices that invite or conceal fraud. Regulation can also deter migration of undesirable individuals into positions of trust or substantial financial responsibility.

In the United States, all federally insured financial institutions are required by law to file reports with law enforcement agencies whenever they have reason to believe that crimes may have occurred at the institutions. The federal bank regulatory agencies recently revised the reporting procedures to incorporate the benefits of information technology. Under the revised system, known as the Suspicious Activity Report (SAR) system, the reports are filed at one central point where they are entered into a computer database. Law enforcement agencies access the SAR database and retrieve all SARs for their respective jurisdictions. In addition, the computerized database enables law enforcement and regulatory agencies to analyze the SARs and identify emerging crime trends.

(ii) *Regulation of Currency Transactions*

Because money laundering facilitates criminal activity, Congress enacted statutory provisions that create a paper trail for currency that resembles the document trail created by other financial transactions involving bank cheques and money wire transfers. Essentially, the legislation creates reporting requirements when currency enters or leaves the country and whenever cash transactions take place at banks and certain other businesses.

On the international level, several organizations are engaged in sponsoring money laundering enforcement programs. The Financial Action Task Force (FATF), an organization comprising of twenty-six nations, issued revised recommendations in 1996 that broadened the scope of the original recommendations to include monies derived from all serious crimes and to mandate the reporting of suspicious transactions by financial institutions. FATF also conducts mutual evaluations and assessments of member states' anti-money laundering measures by representatives from fellow members.

The United Nations Global Program Against Money Laundering (GPML), based in Vienna, Austria, uses technical cooperation and research projects aimed at providing member states with the means to combat money laundering. GPML is working with other international organizations to develop an Internet website on money laundering matters, including a database of law and regulations.

110TH INTERNATIONAL TRAINING COURSE
VISITING EXPERTS' PAPERS

A relative of the credit card, the stored value or smart card, may someday replace currency entirely. But the stored value card adds another dimension to money laundering. Simply loading the stored value card with a value of \$5 million in credit renders it the functional equivalent to several suitcases of hard currency.

(iii) *Coordination and Working Groups*

The presence of government regulation is an important step in helping to protect an industry or sector of a country's economy. To maximize the benefits of regulation, however, another ingredient must be added, coordination with the law enforcement community. We have found that interagency bodies, which we call working groups, are an effective means of developing and maintaining that coordination. For example, during our recent savings and loan (S&L) crisis, we relied heavily on our national Interagency Bank Fraud Enforcement Working Group to ensure that our law enforcement and regulatory communities were working in tandem to fight fraud against our financial institutions. In addition to the Bank Fraud Working Group, the Department of Justice currently maintains at least five other working groups for insurance, health care and telemarketing fraud, as well as for money laundering and securities and commodities fraud.

III. TRENDS AND STRATEGIES

A. The Challenges of the Next Decade

Many of today's fraud schemes are simply repackaged versions of classic frauds. We can expect, however, that

tomorrow's frauds will continue to embrace advances in technology and to exploit gaps created by the absence of international agreements and coordination.

(i) *Cybercrime*

Cybercrime, a term that has come to embrace computer-related crime and other high-tech offenses, seems certain to be the crime of the next decade. Computers may be used as a storage or communications device in the execution of a fraud scheme. As an example, a fraudulent telemarketing firm could store names and relevant data concerning prospective victims to be telephoned in a systematic execution of the scheme.

Computers may be used more directly in the scheme as an instrumentality of crime, a tool facilitating the fraud. For example, personal computers have been used successfully to gain unauthorized entry into bank computer systems and then to transfer bank funds to accounts controlled by the cyber-criminals.

The computer also serves as a weapon for the theft of data, telephone or computer services, or for damage to computers and communications systems. Recent media reports described precautions being taken by some governments against the threat of a computer terrorist attack on vital parts of a country's infrastructure.

B. Effective Countermeasures

1. Prevention

The United States Attorney General has placed high priority on crime prevention. In the white collar crime arena, this is an especially cost-effective approach to fighting crime. It has great potential not only to prevent billions of dollars in fraud

losses but also to conserve precious law enforcement resources.

Crime prevention enlists the private sector and citizens in the campaign to fight economic crime. The preventive measures need not be expensive or rely heavily on high-tech solutions. Our experience with prevention programs suggests great promise. For example, the banking industry, plagued by mounting losses from counterfeit cheque schemes, recently adopted a straightforward preventive measure. When a non-customer seeks to cash a cheque, the bank requires that the non-customer place his/her fingerprint on the cheque using an inkless fingerprint pad. In states in which this practice has been adopted, cheque fraud has been reduced by 60% or more.

Credit card companies are experiencing success in fighting fraud through the use of neural network technology that uses computers to track individual cardholder spending habits. Visa reported this year that fraud, as a percentage of volume, reached an all-time low in 1997 as a result of the neural network and related fraud detection measures. "Smart" cards, the next generation of credit cards, employ embedded computer chips to store a wealth of information about the cardholder, including biometric information that includes the cardholder's physical characteristics.

Government benefit fraud has been reduced through the use of electronic benefit cards that create a computer trail to detect illegal usage of the welfare benefits.

2. International Cooperation

The Global Community has come to realize the critical need for coordination and cooperation in meeting the threat of global economic crime. Some groups, like

UNAFEI, operate under the auspices of the United Nations. Others are based on regional or economic relationships. Although their precise missions may differ, all of these organizations share one common goal, ensuring that borders do not remain barriers to effective law enforcement cooperation.

3. Training

Training is an essential ingredient in mounting a successful law enforcement response to economic crime. White collar criminals are clever and resourceful and often operate in sophisticated segments of industry and finance. Moreover, many white collar crimes occur in regulated business environments. Investigators and prosecutors require specialized training in order to navigate these difficult areas.

Commerce is exploding on the Internet. Stocks can be bought and sold, merchandise and airline tickets purchased, and banking transactions conducted from the home personal computer. Our law enforcement agencies must expect financial crime to gravitate to the Internet as it becomes the global marketplace. Thus, investigators and prosecutors will face difficult issues, both technical and legal, as we confront cybercrime. Only through formal, structured training programs will we be able to develop the necessary expertise to meet the challenge.

IV. THE FUTURE : PROMISING OR PROBLEMATIC?

As we prepare to enter the new millennium, the law enforcement community faces the dual challenges of ever-evolving economic crime and technological innovation that constantly accelerates the pace of change in the Global Economy. Technology serves as a powerful tool in the hands of criminals, but it also can be a devastating weapon against these same criminal forces. Through training

110TH INTERNATIONAL TRAINING COURSE
VISITING EXPERTS' PAPERS

and professional development of investigators and prosecutors, the law enforcement community can continue to suppress the global white-collar crime threat. International cooperation and coordination are central to enforcement responses and to ensuring that a tidal wave of global crime does not engulf the many benefits of the Global Economy.