

MARITIME LAW ASSOCIATION

OF

AUSTRALIA AND NEW ZEALAND

NINTH ANNUAL CONFERENCE

Singapore

4th - 9th July, 1982

PREVENTION OF MARITIME FRAUD -
SOME OBSERVATIONS

by

E.C. FOENANDER

Deputy Public Prosecutor and Senior State Counsel,
Attorney-General's Chambers, Singapore.

The term "maritime fraud" is a composite description of a phenomenon which involves a variety of frauds that include, in the main, charter party frauds, scuttling frauds, documentary credit frauds, and others, either committed individually or in a combination of any two or more of such frauds. Any one type of maritime fraud is an interesting subject and instances of each can provide different insights into the factors that help influence the commission of such crimes.

2. What is proposed to be discussed in this paper, however, concerns more of documentary credit frauds with some observations on certain factors that seem to have encouraged their perpetration. An example of such a fraud will be outlined to illustrate this and the modus operandi adopted by the fraudsters. No doubt there will be other variations used elsewhere. It should be noted too, that this type of maritime fraud - documentary credit fraud - appears to be particularly prevalent in Singapore in comparison to the other types of such fraud briefly referred to earlier. It is, consequently, the type of maritime fraud that is most actively investigated here and, in recent times, prosecuted in the Courts with some measure of success. The solution to this problem is by no means nearby in sight although it must also be acknowledged that the pressures exerted by continuous investigations by the police have certainly not encouraged any wide scale incidence of such crimes. Its continued presence however, can be attributed largely to the attraction of the enormous spoils that these crimes promise, if successfully perpetrated, as well as to certain other factors that prevail in international trading that appears to facilitate their perpetration.

3. Documentary credit frauds may range from the crude to the highly sophisticated, in terms of the modus operandi used. In the former may be included the instance where the shipper forges one of the many shipping documents, say, a certificate of purity, in respect of inferior goods which he intends to ship to another country in place of the actual goods he has contracted to supply. Alternatively, he may forge a Bill of Lading in respect of the number of items of cargo he has shipped to that other country. Such frauds will surface soon enough or, at the latest, when the consignee takes delivery of the cargo and eventually discovers the true nature and quantity of the goods he has received as against what is reflected in the relevant documents in his possession. In such an instance the perpetrator of the fraud will not be too difficult to identify. His apprehension will depend, of course, on whether he has had the presence of mind to abscond earlier. If he has not absconded, his apprehension will then depend on the extent of cooperation between the law enforcement agencies of the two different jurisdictions concerned and the priority of the crime vis-a-viz these agencies.

4.1 In the more sophisticated maritime fraud, a great deal more of detective work will need to be carried out by the law enforcement agency concerned to expeditiously uncover the fraud and collect the requisite evidence to support a prosecution. Concerted efforts must also be made to identify and to apprehend the fraudsters responsible for the crime without any delay. Such a fraud sometimes comprises a combination of frauds involving documentary credits, false insurance claims, scuttling of vessels, and others which would call for more extensive investigations.

4.2 For an example, I would outline the following facts. Take X, a dishonest shipper, who intends to cheat a bank (A) of vast sums of money through the use of false documents in the negotiation of documentary credits. Firstly, he incorporates and registers a private limited company (B). This is quite easily done here where a minimum registration fee of only \$300.00 is required, depending on the authorised capital of the company. He holds the position of Chairman in this company while an accomplice is registered as a director. Next, X opens a current account with Bank A in the name of his company, i.e. Company B. Thereafter, for the first year or so of the operation of his company, X transacts legitimate business which includes the supplying of goods to overseas customers which also involves the negotiation of Letters of Credit through Bank A. Eventually, after establishing an active working relationship with Bank A, he applies for and obtains overdraft facilities - for a modest limit - for his company with Bank A. In the meantime he has cultivated a close working relationship with the Managing Director (Y) of a large company (C) who, coincidentally, also operates a current account, with extensive credit facilities, with the same bank (BankA). He (X) has occasionally utilised the facilities of Company C to open Letters of Credit on his Company's behalf in order to transact business with overseas customers when his company's own credit facilities with Bank A were found to be inadequate to effect this. Y, on behalf of his Company C, acceded to this arrangement for a consideration in the way of a commission that would be paid to his company by Company B, based on the value of the Letter of Credit as and when these were required (by Company B). As far as Bank A is concerned both Company B and

Company C are valuable customers carrying on legitimate businesses. Bank A is also aware of the relationship between the two companies and also of the fact that Company C has in the past indirectly "financed" Company B by opening Letters of Credit in the latter's favour to pay for goods that it (Company B) has contracted to supply to its overseas customers. It (Bank A) permits this working relationship to exist because it (Bank A) also levies a commission and other charges on every Letter of Credit that Company C opens in favour of Company B. The next step that X does is to collaborate with Y in a plan where by contracts on C.I.F. terms for the supply of a variety of goods valued up to \$10 million would be obtained by both their companies from overseas customers. He also obtains contracts for his company (Company B) to supply goods to other overseas customers on a "documents against acceptance" basis. These contracts are for goods valued at \$5 million. These goods will be shipped on board a vessel to be purchased by Company E, a shipping company, of which X is also its Chairman. The price of the vessel F is \$1 million. Company E does not have the funds to purchase it but X (in his capacity as the Chairman of Company E) arranges with Bank A to open a Letter of Credit in favour of the vendors of the vessel for its price, with this facility (granted by the Bank A) guaranteed by another Company G, whose Chairman is promised a commission by X (on behalf of his Company E) based on the value of the Letter of Credit that Company G has guaranteed. Eventually, following the signing of the aforesaid contracts between Company B and Company C, on the one hand, and its overseas customers, Letters of Credit to the value of \$10 Million are opened by the

latter in favour of Company B and Company C. These are eventually received respectively by the latter two companies.

The vessel F, in the meantime, is on its way to Singapore from Taiwan, from where it was purchased. Before its arrival however, X forges a whole series of documents which will be required for the negotiation of the Letters of Credit that he now has in his possession. For this, he enlists the assistance of several persons in the local trading community with promises of a hefty commission at the end of it. A similar set in respect of company C's Letters of Credit is also prepared on his (X's) instructions. He even involves another Company, which carries on the business of surveying and analysing ships' cargoes, from which he obtains Certificate of Purity and Quality, without having the goods surveyed, on payment of a "fee" to the Managing Director of that Company. Invoices, Packing Lists, Delivery Orders signed by both X and Y, Bills of Lading, Shipping Orders, etc. are all forged with appropriate letterheads to convince Bank A that all the requirements of the Letters of Credit are complied with. The vessel F is still on the high seas but nevertheless X presents the requisite documents with their respective Letters of Credit, on behalf of his Company B and Company C, to Bank A for negotiation. Prior to this he and Y have taken out insurance policies (on behalf of their overseas buyers) on the "goods" that have purportedly been "shipped" on vessel F that is still on the high seas. In respect of the contracts on the "documents against acceptance" bases, X's Company B also takes out insurance policies to cover the "goods" involved on their journey to the

prospective buyers. This was not difficult as the underwriters were content to rely merely on the respective proposals that he and Y have submitted to them earlier without themselves (or their representatives) examining the cargo. X, in addition, also takes out hull insurance on the vessel F in his capacity as the Chairman of Company E, the owners of the vessel.

4.3 Eventually, the documents submitted to Bank A in support of the Letters of Credit are found to be in order and the documentary credits are accordingly negotiated. The proceeds thereof are paid into Company B's and Company C's current accounts with Bank A. It is only after this that vessel F arrives in port. With the proceeds from the negotiated Letters of Credit X and Y both instruct Bank A to pay various sums totalling \$1 million to Company E. These payments are reflected in the accounts of Company B and Company C, backed with corresponding vouchers, as payments towards the cost of goods purchased from Company E. Eventually, after the amount of \$1 million is paid into Company E's account, it is disbursed by X, in his capacity as the Chairman of Company E, to Bank A in repayment of the \$1 million that Bank A has opened by way of a letter of Credit on its (Company E's) behalf to pay the vendors of the vessel F.

4.4 So, as it stands, X and Y have so far only expended the monies received from their overseas customers (via the Letters of Credit) to purchase the vessel F. As regards the vessel F, X then arranges to have it loaded with barrels of sand and other crates containing earth or stones to resemble the cargo described in the respective Bills of Lading and other documents as well as to present the respectable fiction

that the vessel F is indeed loaded down with the stated cargo. X also arranges for a fresh crew comprising various nationalities to be recruited for the vessel as well as a reputed "scuttler" who assumes the position of Chief Engineer of the vessel. The vessel then sails for its purported destination. However, while on the high seas, at night, and according to plan, in a part of the ocean where it is deepest and where other vessels are bound to ply, the vessel F is scuttled and takes water. The crew board lifeboats and are rescued subsequently by another passing vessel. Vessel F takes its time to go fully under but not before everyone in the vicinity has observed its descent into the watery beyond. The master of vessel F is not aware of the plot and has, in the meantime, radioed an SOS to the owners of the vessel, namely, Company E. Company E receives the message and X personally contracts with a salvage company to undertake rescue measures, knowing fully well that it will be impossible to save the vessel. Sure enough, vessel F has disappeared beneath the waves even before the salvage company's own vessels can reach the scene.

5. Arising from the scuttling of the vessel F, and barring any investigation into the event, the following would have resulted:-

- (a) The Letters of Credit worth \$10 million will have been negotiated and the proceeds - less the expenses incurred by X and Y, e.g. payments towards the bogus cargo, the purchase of the vessel F, the payments of insurance premiums, and such - would now be held in the accounts of Companies B and C;

- (b) X would be in a position to lodge a claim against the insurance companies who under wrote the policy covering the hull insurance taken out on the vessel F;
- (c) X would be in a position to lodge claims on the policies taken out by underwriters to cover the cargo worth \$5 million in respect of the contracts on a "documents against acceptance" basis.

So far neither X nor Y have incurred any expenses of their own in this scheme. All expenses would have been taken care of from the proceeds of the Letters of Credit. These would include those relating to the purchase of the vessel F, the insurance premiums paid on the several policies taken out, the cost of the bogus cargoes, the freight charges and such. Appropriately forged vouchers and receipts would be in abundance to cover the purported purchases of "supplies" from the suppliers of the cargoes in question and the other "payments". "Freight charges" paid to Company E in respect of the "cargo" on board the vessel F would similarly be supported by relevant documents and receipts. In actual fact the said "freight charges are" merely a circuituous means to channel proceeds from the fraud to X, who is also the Chairman of Company E.

6. It is surmised that in the above situation the fraud could have been nipped in the bud if certain of the innocent participants in the whole transaction had exercised more caution in their dealings in such transactions. Bank A, for example, could have been more vigilant and noticed the unusually large orders that the relatively small Company B has lately

received. The purchase of the vessel F by Company E of which X - the Chairman of one of the shippers, Company B - was also the Chairman, would have provided a pointer as well. It could further have taken the simple expedient of verifying with the port authorities of the presence in port of vessel F, as indicated in the Bills of Lading presented. Had this been done the fraud would have been exposed and the fraudsters dealt with. The Delivery Orders signed by X and Y -if forming part of the documents required for the negotiation of the Letters of Credit in question -would also show that they were issued by Company E, a shipping company, and not one that dealt in such commodities that were purportedly shipped on vessel F. On the other hand, the underwriters who issued the insurance policies in respect of the cargo in question, could have taken steps other than relying merely on the proposals (for insurance) submitted by Company B and Company C before agreeing to issue the requisite policies. The enormous value of the cargo, for instance, would be reason enough for the insurance companies to exercise a greater degree of prudence by stipulating for the engagement of an approved surveyor to survey the cargo before taking on the risk. To rely on certificates or reports issued by a survey organisation that is appointed by the shippers themselves may well be a convenient and universally accepted practice. However, in the light of the currently rising incidence of maritime frauds any continued reliance on such a practice may well be foolhardy unless the shipper concerned is a trusted and reliable client. In this respect, it should be noted that the grandiose scale on which maritime frauds are being committed in recent times rules out the management of the fraud being attributed to only one person. There must necessarily be others involved

and where the conditions in a Letter of Credit include one that calls, say, for a surveyor's report or certificate, without stipulating any particular surveyor, it would be quite probable that the principal fraudster will not only collaborate closely with but will also recruit as an accomplice the surveyor that he chooses to use for the purposes of his fraud. Hence, the need for greater prudence.

7. With regard to the role of Bank A, it is anticipated that the stock answer would be that banks "deal in documents and not in goods" and as long as these are in order there is no further obligation or duty on them to execute further checks on the validity or otherwise of the documents presented for the negotiation of Letters of Credit. Without doubt, Articles 8 and 9 of the Uniform Customs and Practice for Documentary Credits (see 1974 Revision) will be held aloft confidently as a defensive shield in this respect. It should be noted too, that added to this "protection" is the assurance enjoyed by negotiating banks in general that a full reimbursement for any advances released on a negotiated Letter of Credit will be made by the credit opening bank concerned. In such circumstances it can hardly be expected of such banks to do more than what is required of them under the Uniform Customs and Practice for Documentary Credits. It is observed however, that this has presented the perfect setting for the perpetration of such frauds. The fraudster would need only to prepare a set of flawless (but forged) documents and present it to the negotiating bank without a thought that it will inquire further into their validity at all. Banks also repeat the notion that with the many documentary credits that are presented daily for negotiation any additional

checks on the validity or otherwise of those and their associated documents would be almost impossible without slowing down the flow of such transactions. This is a misapprehension. While it is not being advocated that banks should thoroughly check the validity of each and every document presented to support the negotiation of a Letter of Credit, it is instead proposed that other aspects may yet be verified without dislocating the normal procedures that are followed daily. There has in fact been an instance where a vessel named in a Bill of Lading was subsequently discovered to be non-existent and nowhere in port, and yet a Letter of Credit had by then been negotiated and the proceeds spirited away. Another instance involved the Exports Manager of a bank, but with different, and more comforting, results. He noticed that two shippers, who had submitted two separate sets of documents to negotiate Letters of Credit, had only recently opened separate current accounts with his bank and also shared a common signatory to the accounts. He also noticed that the Letters of Credit in question were in respect of large purchases of a certain commodity by overseas traders, which was unusual, as the two local shippers had never before received such lucrative orders. A further check revealed that both these shippers occupied the same office in a certain building. He also noted that both the shippers were using the same vessel that was scheduled to convey the cargoes involved. Going further, he checked again on the vessel and discovered that it had been lying at anchor in harbour for the past four months or so without venturing anywhere. Now thoroughly aroused, he refused to negotiate the Letters of Credit but not before discreetly reporting his suspicions to the Commercial Crime Division of the

Police. The Police moved fast and true enough, on boarding the vessel and locating the purported cargo concerned with the questioned Letters of Credit, they discovered, on breaking open the crates and packages which purportedly held the said cargo, that they contained worthless articles that could never have fitted the description of the cargo described in the related Bills of Lading, etc. The shipper was promptly arrested, charged in Court and eventually convicted for engaging in a conspiracy to attempt to cheat the bank whose alert Export Manager had been the first to identify the tell-tale signs of the fraud in the offing.

8. It is acknowledged that the scale on which maritime frauds are committed and their wide-spread prevalence internationally, taken together with the magnitude of present day international maritime trade, makes it merely an ideal to hope for the outright eradication of this scourge. A more pragmatic approach is to exhort all parties to international maritime trade transactions to sit up and be more vigilant in their dealings with each other instead of rushing headlong into a deal in anticipation of quick profits. Even the observance of simple precautions may achieve more towards prevention than the setting up of elaborate and formal checks and balances. The role of the government in the aim to combat the increase of such frauds is of paramount importance as well. Its various departments can be co-ordinated with this aim in mind and the exchange of expertise and information between each other would be invaluable towards that end. Combining such efforts with the expertise from those quarters engaged in international maritime trade should provide a potent mix to enable such frauds to

be detected earlier and the fraudsters apprehended. The existence of such a combined force would itself be a deterrent to discourage, at least, a higher incidence of such crimes. The incidence of such crimes must also be publicised and recognised for its debilitating effects, not only on the immediate parties involved in a transaction, but also on the ultimate consumer as well. The prosecution and punishment of those responsible for the perpetration of these frauds must also be made known widely if only to effect a deterrent influence on other would-be perpetrators. At the same time it should always be remembered that frauds of this nature are not confined to any one country but are of international dimensions. Logically, therefore, effective inter-governmental co-operation in the matter must be attained. Police forces of different countries, for example, must co-operate in real terms with each other in the exchange of intelligence and the granting of practical assistance to the other when relevant evidence for, say, a prosecution, is sought. This may be effected on an informal basis instead of proceeding via formal channels which may result in unnecessary delays and the frustrating prospect of the "bird flying the coop" before he can be brought to book.