Red Flag Indicators on Trade-Based Money Laundering

Introduction

Trade-based money laundering (TBML) generally involves the exploitation of complex cross-border financial instruments which are used to export and import goods, to launder illicit funds, with the involvement of different parties and jurisdictions. Whilst financial institutions providing a range of trade-based services to their customers, TBML is often hidden among genuine trade activities across entities and geographies, adding to the challenge of detection.

TBML has been identified as the third most significant unlawful activity that generates criminal proceeds in Sri Lanka and poses 'Medium High' money laundering threat. Therefore, the financial sector of Sri Lanka has a significant role in the detection, reporting and disruption of TBML.

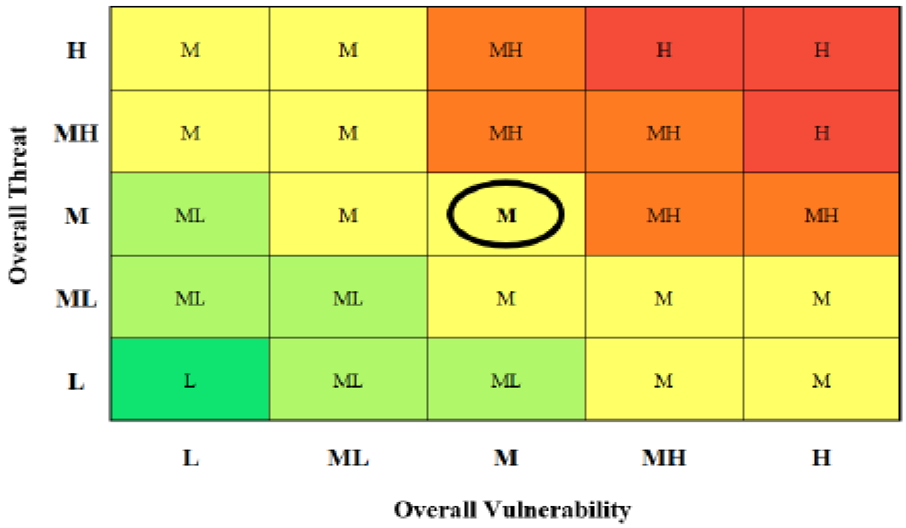
Summary of NRA Findings

National Risk Assessment (NRA) of Sri Lanka on ML/TF 2021/22 was conducted by the Financial Intelligence Unit (FIU) of the Central Bank of Sri Lanka (CBSL) together with public and private sector stakeholders. The assessment was aimed at identifying the ML/TF risks in the country and highlights the most significant ML/TF threats, vulnerabilities, and risks faced by Sri Lanka.

Identified ML Threats of Sri Lanka

Predicate Offence	ML Threat
Drug trafficking	Medium High
Bribery and corruption	Medium High
Customs related offences including laundering of trade-based proceeds	Medium High
Fraud	Medium
Robbery	Medium
Environmental and natural resource crimes	Medium
Human smuggling/trafficking	Medium Low
Tax offences	Medium Low
Illegal, unreported and unregulated fishing related unlawful activities	Medium Low
Counterfeiting of currency	Low

Overall ML/TF Risk in Sri Lanka



As shown above, the 2021/22 NRA has identified TBML as a predicate offence which poses 'Medium High' money laundering threat in Sri Lanka.

Red Flag Indicators

The Financial Intelligence Unit (FIU) wishes to issue the following list of red flag indicators in order to mitigate the risk of TBML in Sri Lanka in addition to the previous list issued on 23.02.2021. These red flags are indicative of the potential risks of TBML, and the financial institutions are required to establish proper systems and controls, based on KYC & CDD, to mitigate the TBML risk and to report suspicious transactions to the FIU.

Trading Activity related indicators

1. The commodities that are traded do not match or are inconsistent with the line of business activities of the customer, e.g. clothing dealer is importing seafood.

2. The traded goods that are reported in the transaction cannot be observed during physical onsite visit/examination.

3. The customer engages in complex trade deals involving numerous third-party intermediaries.

4. Entity is a newly registered or recently re-activated company that is involved in unexpectedly large transactions.

5. The customer and the beneficiary to the transaction are related/connected parties.

6. The customer/potential customer is unfamiliar with the intended use of the product, which is sold by the supplier.

7. Lack of clarity on trade details (date, amount, goods involved, beneficiary names, bank accounts numbers, jurisdictions, foreign entities involved).

8. There is reluctance or refusal on the part of the customer to provide the information, such as the destination of the product, the intermediary details, etc.

9. When large amounts are remitted outside the country for unclear and vague purposes. Eg. for consultancy, online training, software development etc.

Documentation related indicators

10. Misrepresentation or significant discrepancies in the description, quality, quantity, invoices, and/or prices that are inconsistent with market value and/or origin of the goods on the documents.

11. The commodities are misclassified or in other words, an incorrect Harmonized System (HS) commodity classification code is declared, to avoid reporting or for false reporting to the customs in order to avoid taxes and duties (e.g., high-value commodities) or to circumvent prohibitions and restrictions on transnational trade, (e.g., narcotics and other illicit drugs, dual-purpose goods etc.).

12. The commodities are over-or under-valued in the documents related to the transactions, e.g. proforma invoice, commercial invoice.

13. The transactions involve double invoicing or multiple invoicing for the same consignment.

14. Use of shell companies in documents e.g. agreements of sale/purchase.

15. Foreign entities use identical invoices and/or addresses, indicating a possible connection and/or third-party control.

16. Documents relating to trade or customs declarations are appeared to be frequently modified, amended or counterfeited.

Payments and settlements related indicators

17. The payment to the vendor is made by unrelated third parties.

18. Companies receiving third party payments where the originator is an entity located in a country unrelated to the trade transaction.

19. The customer prefers to pay cash even if they qualify for open credit terms.

20. The suggested method of payment of the customer is inconsistent with the risk characteristics of the transaction.

21. The customer changes the method of payment at the last minute.

22. Business account funded by cheques and wire transfers from multiple domestic and international entities citing payments for goods/services that appear to be unrelated to the focal entities' line of business/sector.

23. There are frequent amendments to letters of credit or there may be concerns about the contents of the activity or information connected to the letter of credit. e.g., change of commodity description, change of the type of transaction from Sale to Transshipment or Entrepot trade.

24. Use of generic purpose of payment texts with same or different parties such as “for goods”, “for equipment”, “for materials” “for intermediary purposes” etc.

25. Payments for goods are routed through several intermediary jurisdictions, including high-risk jurisdictions (such as tax havens and bank secrecy jurisdictions) without economic rationale.

26. The funds are transferred through one jurisdiction, while the traded goods are shipped between unrelated jurisdictions without a reasonable explanation for the business model.

27. Payments are routed in a circle. Funds are sent out from one country and received back in the same country, after passing through another country or countries.

28. An importer regularly fails to settle the funds to the exporter on the consignment’s importer under Open Account terms and D/A Terms.

29. Receipt of large amount of export proceeds appear inappropriate when consider the volume of exports.

30. The entities frequently remit funds as advanced payments to foreign suppliers of goods based on proforma invoices which are apparently containing improper details of the goods and unauthentic authorization.

Consignment related indicators

31. Repeated importation and exportation of the same high-value commodity, without a proper economic rational.

32. The commodities involve improbable goods, origins, quantities, destination.

33. The parties use unusually long shipping routes or transshipment points to carry and handle the commodities that can be easily sourced from a much closer supplier.

34. Transshipment through one or more jurisdictions with no apparent economic reason.

35. The product raises doubts given the intended shipping destination or buyer.

36. Importing of Intangible commodities such as software, intellectual property rights which are incapable of being measured, but revealed through contract documents.

37. The method of packaging is inconsistent with the commodity or shipping method.

Other Indicators

38. Customer remains unresponsive after being inquired by financial institution on certain transactions and/or may stop business through certain accounts after being inquired by the financial institution.

39. A trading entity, its owners, or senior managers, appear in negative news.

40. The name of a trading entity is similar to the name of a well-known corporation, even though it is not actually connected, rather is an effort to appear as a part of such well-known corporation.

41. Address of the company is an incomplete address and suspected to be non-existing.

42. Numerous sole proprietorships or private limited companies engaged in trading activities are controlled by the same group of people.

43. When the Directors of the Company or their employees often request large amount of foreign currencies for their overseas travel.

44. When an enforcement agency (Customs, Police, IRD etc.) requests information and/or documents of an entity for an investigation.

Disclaimer: Please note that the above is not an exhaustive list of possible indicators of transactions relating to TBML. Accordingly, you are required to have robust CDD processes in place to identify these red flags and report suspicious transactions to the FIU. You are also required to train the staff to be vigilant in detecting potential TBML activities and to establish clear policies and procedures to address these issues. Therefore, Financial Institutions are required to take note of these red flags indicators to take appropriate actions to reduce the possible TBML risks, if any.