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RED FLAG INDICATORS FOR PROLIFERATION FINANCING (2020)

1. WHAT IS PROLIFERATION?

The definition of **"Proliferation"** provided in the FATF's 2008 Proliferation Financing Report [1]is: "Proliferation has many appearances but ultimately involves the transfer and export of technology, goods, software, services or expertise that could be used in nuclear, chemical or biological weapon-related programs, including delivery systems; it poses a significant threat to global security."

The Report, which identifies a link between proliferation of Weapons of Mass Destruction (WMD) and terrorism, states that: "If appropriate safeguards are not established, maintained and enforced for sensitive materials, technology, services and expertise, they can become accessible to individuals and entities seeking to profit from the acquisition and resale, or for intended use in WMD programs".

2. WHAT IS PROLIFERATION FINANCING (PF)?

The 2010 FATF's Guidance on Counter Proliferation Financing [2] defines "**Proliferation Financing"** as:

"the act of providing funds or financial services which are used, in whole or in part, for the manufacture, acquisition, possession, development, export, trans-shipment, brokering, transport, transfer, stockpiling or use of nuclear, chemical or biological weapons and their means of delivery and related materials (including both technologies and dual use goods used for non-legitimate purposes), in contravention of national laws or, where applicable, international obligations".

The said report further adds that:

"PF facilitates the movement and development of proliferation-sensitive items and can contribute to global instability and potentially catastrophic loss of life if weapons of mass destruction (WMD) are developed and deployed".

3. INTERNATIONAL STANDARDS AND OBLIGATIONS TO COUNTER PROLIFERATION FINANCING RISKS

- **The United Nation Security Council's Resolution (UNSCR 1540)**

  On April 28, 2004 the UN Security Council adopted UNSCR 1540, which was established to prevent non-state actors from acquiring nuclear, biological, and chemical weapons, their

[1] FATF PROLIFERATION FINANCING REPORT
https://www.fatf-gafi.org/media/fatf/documents/reports/Typologies%20Report%20on%20Proliferation%20Financing.pdf

[2] FATF GUIDANCE ON COUNTER PROLIFERATION FINANCING
http://www.fatf-gafi.org/media/fatf/documents/reports/Guidance-Countering-Proliferation-Financing.pdf

means of delivery, and related materials. The resolution filled a gap in international law by addressing the risk that terrorists might obtain, proliferate, or use WMDs. The UNSCR 1540 imposed the following three (3) primary obligations upon its UN membership (including Pakistan) to restrict proliferation financing. The financial provisions of the Resolution require that all States:

a. abstain from supporting non-State actors seeking WMDs and their means of delivery;
b. adopt and implement effective laws (i.e. criminal or civil penalties for violations of export control laws) to prohibit non-State actors from developing, acquiring, manufacturing, possessing, transporting, transferring or using nuclear, chemical or biological weapons and their means of delivery; and
c. establish and enforce effective measures and domestic controls (i.e. export and transhipment controls) to prevent the proliferation of nuclear, chemical, or biological weapons, their means of delivery and related materials.

- The Financial Action Task Force (FATF) Recommendations & Immediate Outcomes

Recommendation 7 of the FATF Standards requires countries to implement proliferation financing-related Targeted Financial Sanctions (TFS) made under United Nations Security Council Resolutions (UNSCRs or resolutions). Recommendation 2 requires countries to put in place effective national cooperation and, where appropriate, coordination mechanisms to combat the financing of proliferation of weapons of mass destruction (WMD). Immediate Outcome 11 and certain elements of Immediate Outcome 1 relating to national cooperation and coordination aim to measure how effective countries are implementing these Recommendations.

4. Pakistan's Regulatory Framework for Combating Proliferation Financing

To address the risk of proliferation financing and to comply with the above requirements of UNSCR 1540 and FATF's Recommendations and Immediate Outcomes, Pakistan has established relevant legislations, regulations and guidelines which include but not limited to following:

- Anti-Money Laundering Act 2010 (as amended up to Sep 2020);
- Anti-Terrorism Act 1997;
- United Nations (Security Council) Act, I948;
- State Bank of Pakistan's AML/ CFT/ CPF Regulations (Issued on 30 Sep 2020);
- AML / CFT Regulations Issued by SECP;
- Federal Board of Revenue AML/CFT Regulations for DNFBPs, 2020;

- National Savings (AML and CFT) Regulations, 2020;
- ICAP's AML / CFT Regulations for Chartered Accountants Reporting Firms; and
- ICMAP's AML / CFT Regulations for Cost Accountants Reporting Firms.
- Guidelines on TFS and UNSC Resolutions by AML / CFT Regulatory Bodies.

Moreover, Strategic Export Control Division (SECDIV), Ministry of Foreign Affairs of Pakistan has also issued detailed guidance document namely "Guidelines on the Implementation of the UN Security Council Resolutions Concerning Targeted Financial Sanctions on Proliferation Financing"[3].

5. Red Flags Indicators for Proliferation Financing

To identify a suspicion that could be indicative of proliferation financing activity, FMU has prepared the red flags indicators that are specially intended as an aid for the reporting entities. These red flags may appear suspicious on their own; however, it may be considered that a single red flag would not be a clear indicator of potential proliferation financing activity. A combination of these red flags, in addition to analysis of expected overall financial activity, business profile may indicate towards potential proliferation financing activity.

Customer Behavior:

1. When customer is involved in the supply, sale, delivery or purchase of dual-use, proliferation-sensitive or military goods, particularly to higher risk jurisdictions.
2. When customer or counter-party, or its address, is the same or similar to that of an individual or entity found on publicly available sanctions lists.
3. The customer is a research body connected with a higher risk jurisdiction of proliferation concern.
4. When customer's activities do not match with the business profile provided to the reporting entity.
5. When customer is vague about the ultimate beneficiaries and provides incomplete information or is resistant when requested to provide additional information.

[3] GUIDELINES ON THE IMPLEMENTATION OF THE UN SECURITY COUNCIL RESOLUTIONS CONCERNING TARGETED FINANCIAL SANCTIONS ON PROLIFERATION FINANCING
http://secdiv.gov.pk/uploads/CRMC_Guidelines_on_TFS_for_PF-38da.pdf

6. When customer uses complicated structures to conceal connection of goods imported / exported, for example, uses layered letters of credit, front companies, intermediaries and brokers.
7. When a freight forwarding / customs clearing firm being listed as the product's final destination in the trade documents.
8. When final destination of goods to be imported / exported is unclear from the trade related documents provided to the reporting entity.

Transactional Patterns:

1. Project financing and complex loans, where there is a presence of other objective factors such as an unidentified end-user.
2. The transaction(s) involve an individual or entity in any country of proliferation concern.
3. The transaction(s) related to dual-use, proliferation-sensitive or military goods, whether licensed or not.
4. The transaction(s) involve the shipment of goods inconsistent with normal geographical trade patterns i.e. where the country involved does not normally export or import or usually consumed the types of goods concerned.
5. Over / under invoice of dual-use, proliferation-sensitive or military goods, trade transactions.
6. When goods destination/shipment country is different from the country, where proceeds are sent/ received without any plausible reason.

Disclaimer:

These red flags are developed for guidance purpose and may appear suspicious on their own; however, it may be considered that a single red flag would not be a clear indicator of potential PF activity. However, a combination of these red flags, in addition to analysis of overall financial activity and client profile may indicate a potential PF activity. While every effort has been made to ensure the accuracy and check all relevant references/ resources, errors and omissions are possible and are expected. Financial Monitoring Unit (FMU), its officers and its stakeholders are not responsible for any mistakes and/or misinterpretation.