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Trade finance
Understanding the financial crime risks

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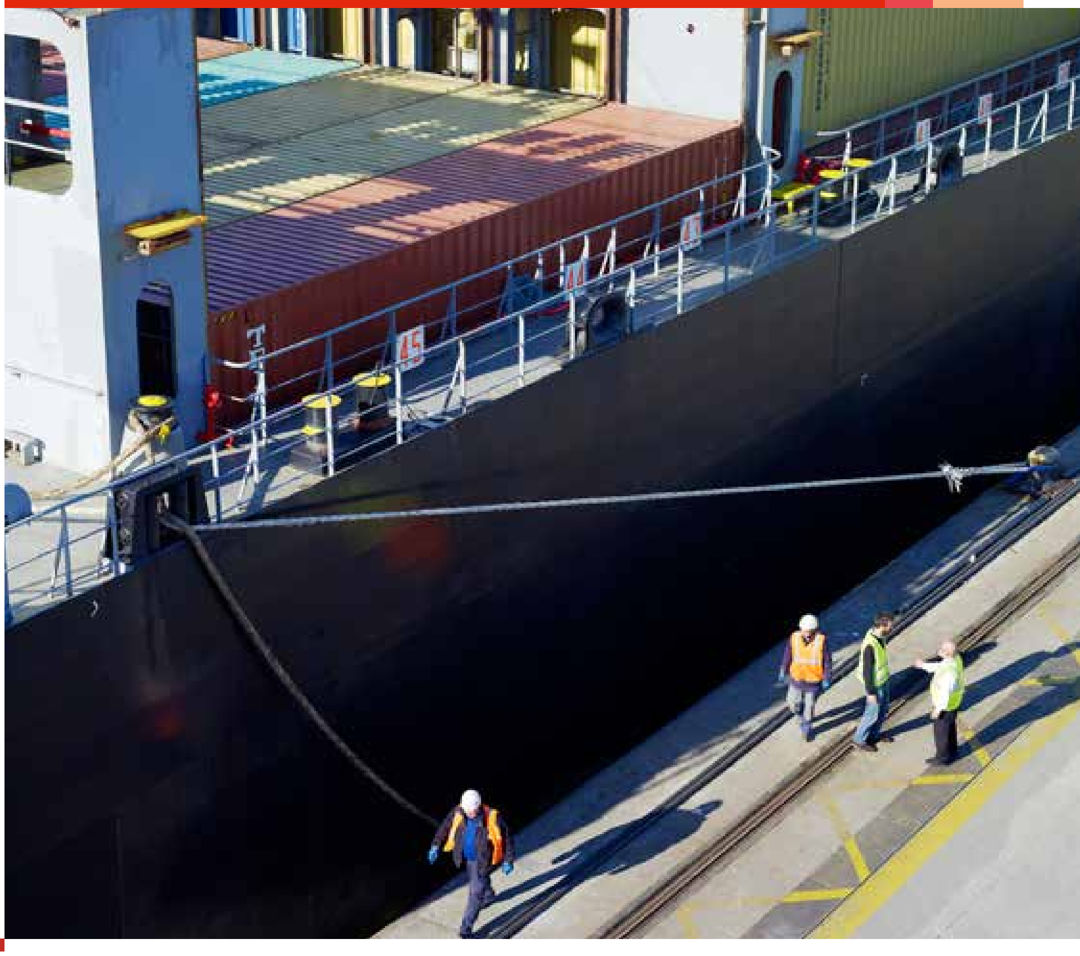
POLE STAR



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Trade finance and financial crime

Between 80-90% of the world's international trade is reliant on trade financing. The process, whereby a bank in the importer/buyer's territory issues a letter of credit to a bank in the territory of the exporter/seller of the goods, enabling the exporter to release the goods, is fundamental to the world economy.

Trade finance has been identified as a potential conduit for money laundering and it has increasingly come under the spotlight as a means of breaching sanctions regulations. This has been brought into focus with warnings and guidance from a number of regulatory bodies; from the Financial Conduct Authority (FCA) to the monetary authorities in Hong Kong and Singapore to the Wolfsberg Group, all calling for regular risk-based due diligence throughout the life cycle of a transaction.

What makes trade finance high risk for financial crime?

Global

The international nature of trade makes it more difficult to manage territory-based risk. Many international banks have set up branches in London to facilitate trade finance activity, and it is important that their compliance functions meet the expectations of UK regulators.

Volume of transactions

Trade finance is a high-volume business involving multiple parties from numerous territories. With the pressure this puts on compliance and regulatory functions, this can present those looking to engage in criminal activities an opportunity to hide their dealings in the mass of activity.

Lack of automation

Trade finance deals are often manually processed and are largely paper-based – especially at smaller and specialist institutions. Effective screening requires experienced individuals that are able to recognise red flags, and with the vast quantity and complexity of information to review, compliance becomes even more challenging.

Dual-use goods

Some 'benign' goods can have dual-use traits, meaning they can be substituted for use in restricted activities e.g. military. Where goods or component parts may be of US origin, institutions may be at the risk of breaching US export control regulations which are extremely prohibitive and complex. Similarly, some sanctions are extremely specific in their details, with fine lines between what is deemed acceptable and restricted. Financial institutions must have appropriately trained personnel that have sufficient familiarity with the nuances of sanctions and other legal obligations to ensure compliance.

Complexity of transactions

Banks screen the applicant, beneficiary, the counter party bank, the transport company, the vessel, the ports and port owners and the goods being transported to identify any sanctions issues. This information is not static and over the course of a transaction could change multiple times – creating due diligence and record keeping challenges. To add further complexity the fair price of goods can often be subjective and difficult to determine, especially as prices can vary across different territories and may be driven by forward contracts.

Ad hoc controls

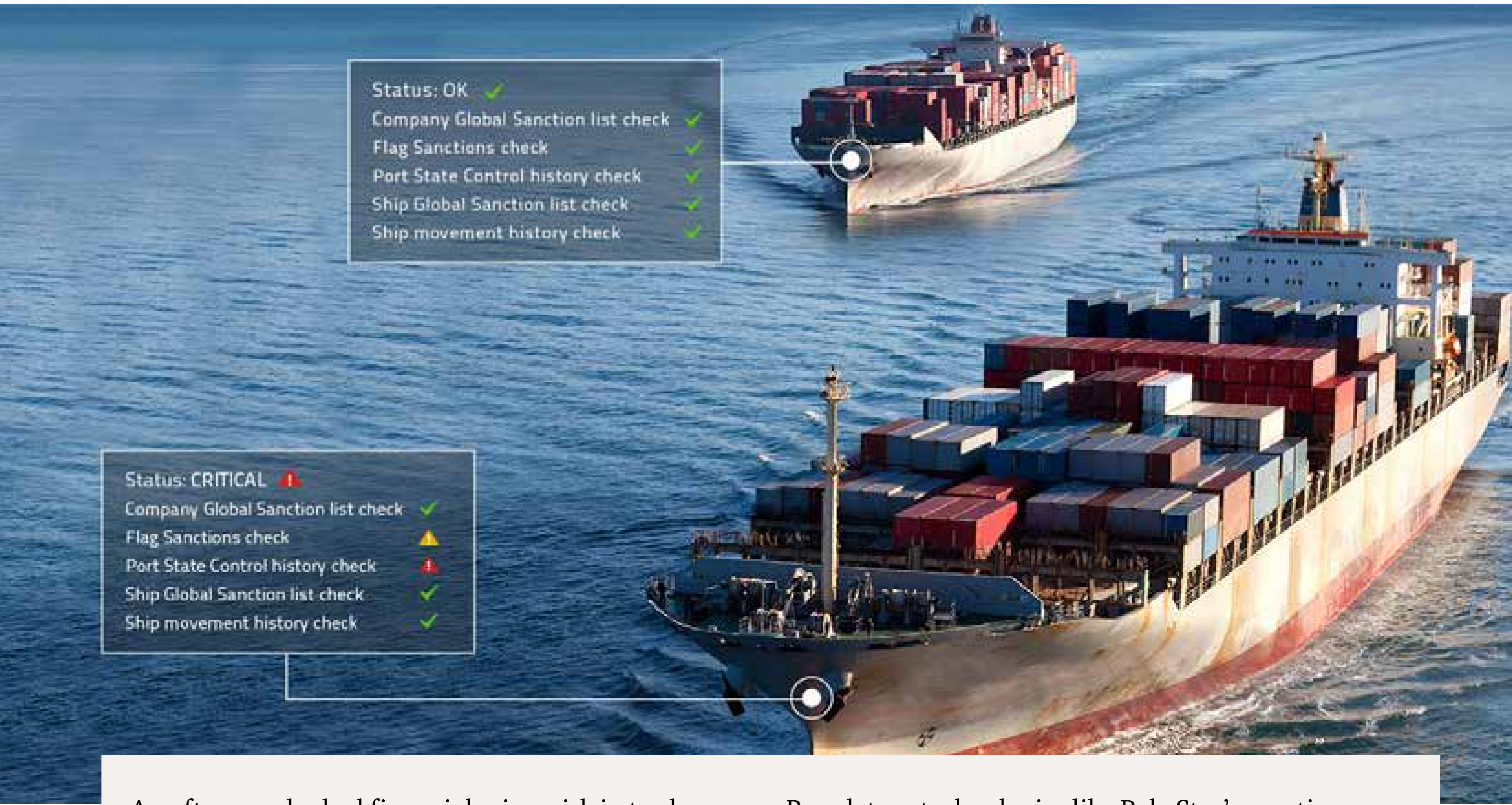
Many financial institutions don't have specific trade-related policies and controls in place. This, added to the likelihood that staff are not receiving adequate training relating to trade finance, can lead to red-flags and risks not being spotted.

Time restrictions

Shipment timings are often set in advance and this lack of flexibility, along with the competitive nature of the trade finance market can put pressure on banks to rush compliance tasks or grant dispensations.

> ***"Trade finance transactions are an attractive medium for money launderers to transfer large values across borders."***
>
> *Monetary Authority of Singapore*

Vessels: A multitude of risks



An often overlooked financial crime risk in trade finance transactions is screening the vessel and the route used. Historically banks have not been performing these screening functions effectively which has led to regulators globally (most noticeably the Monetary Authority of Singapore) codifying the importance of vessel screening and tracking as part of a risk based trade finance compliance programme.

Incorporating vessel screening and tracking into a compliance framework is not an easy task due to the complexity of maritime supply chains, the growing volume and changing level of regulation and the manual nature of most trade finance businesses' compliance processes.

The increasing quantity and complexity of regulations is having a significant operational impact on financial institutions' compliance teams and processes and the need for technology to help solve these compliance challenges is more crucial than ever.

Regulatory technologies like Pole Star's sanctions screening solution for trade finance businesses can help organisations to automate compliance procedures, streamline complex and time consuming procedures and ensure that due diligence and compliance are executed consistently across multiple teams or regions.

Pole Star's solution combines the services a client would normally obtain from separate ship data suppliers; sanction screening databases and vessel tracking systems into one easy-to-use web-based system which generates a tamper-resistant audit trail in seconds, as a record of their compliance activity.

Key benefits of Pole Star solution

- Reveal ships' (and associated entities) exposures to sanctions and regulatory risk
- Provide evidence of sanctions compliance activities
- Reveal historical trading patterns and high-risk ports of call
- Significantly reduce screening time
- Reclaim your team's valuable time
- Demonstrate activities to comply with international regulations
- Protect staff, business and reputation

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Screening

- Screens ships and their associates (including registered and beneficial owner, manager, technical manager) in under 30 seconds
- Screens against a comprehensive set of trade compliance lists (including over 400 economic sanctions, embargoes and denied party lists)
- Screens the ship's associated ownership against OFAC comprehensively sanctioned countries (and any additional countries specified by the user)
- Interrogates Port State Control inspection records
- Generates alerts if a positive match is returned
- Analyses historical movements (up to 12 months) to determine if the ship has recently called at a blacklisted port or sanctioned country
- Identifies ships flying the flag of an embargoed or sanctioned country
- Highlights ships that have entered ports subject to a current geopolitical threat
- Customisable screening criteria

Monitoring

- Blended AIS + Inmarsat secure satellite tracking
- Event detection and alerts
- Daily-re-screening

Audit trail

- Complete audit trail of compliance activities
- Archive data for easy reporting

What are the financial crime risks?

Sanctions

It is possible for entities, individuals, counterparty banks, goods, ports and vessels to be subject to sanctions regimes. Facilitation of trade involving any of the above could result in a breach of sanctions.

Money laundering

Launderers transfer funds by misrepresenting the price, nature, quantity or quality of goods on invoices. Failure to conduct verification can allow inaccurate shipments to pass through and ultimately facilitate money laundering.

Fraud

Complexity, the distance of the banks from the transaction and the documentary nature all make it more difficult for banks to verify the accuracy of the trade activity and information. This makes it easier for fraudulent activity to go undetected.

Bribery and corruption

There are numerous points throughout the lifespan of a trade finance transaction that can be susceptible to bribery activities.

> ***"More work is required at most banks to ensure high-risk customers and transactions are identified and appropriate action is taken by senior management."***
>
> *The Financial Conduct Authority*

How we can help manage risk

With trade and trade finance increasingly being used as a mechanism to facilitate financial crime, it is crucial for institutions to have robust and effective controls in place to manage their regulatory and reputational risks. At PwC we believe that it is essential for institutions to understand the financial crime risks and use technology effectively to help solve their compliance challenges.

The PwC – Pole Star strategic alliance will allow clients to benefit from PwC's leading corporate experience and industry knowledge and Pole Star's maritime intelligence experience and FinTech innovation.

Risk assessment

Review operations to assess financial crime risks and exposure to inform the creation of appropriate risk-mitigating controls.

Strategy and operational design

Perform current state assessment to identify strengths and areas for improvement in your financial crime programme. We will work with you to develop a strategic vision and roadmap to implementation of your target state.

Data integrity and cleansing

Assist in establishing source to screening data lineage methodology to assure data is current, accurate and held in retrievable and usable form.

Enhanced due diligence

Checking names of clients, third parties, vessels, vessel owners and operators against lists of PEPs and sanctioned lists to inform your overall risk position and align with your risk appetite.

Vessel tracking

Tracking vessels can help to alleviate concerns about actual routes taken by vessels versus stated routes. Combining this with a comprehensive screening of the vessel will aid risk management.

Remediation/look back exercises

Review or remediate past activity to identify potential system or process failures and confirm integrity and effectiveness.

Incident response

In the event of a breach, design and implement a response, whether strategic, tactical or remedial, including developing approach, tools and training.

Regulatory response

Coordinate data extraction, remediation and response to meet demanding regulatory deadlines.

Technology review

Review, test and validate the effective operation of screening solutions.

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