



**FINANCIAL INTELLIGENCE CENTRE**  
Combating Money Laundering and Terrorist Financing

# TRENDS REPORT 2014



## Acronyms

- AML Anti Money Laundering
- CDD Customer Due Diligence
- CFT Combating Financing of Terrorism
- CTR Cash Transaction Report
- FIC Financial Intelligence Centre or the Centre
- KYC Know Your Customer
- LEAs Law Enforcement Agencies
- MNE Multi National Enterprise
- ML Money Laundering
- STR Suspicious Transaction Report
- TF Terrorism Financing
- TPM Transfer Pricing Management



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## **FOREWORD**

After one year of operation, the Financial Intelligence Centre (FIC) has played a key role in receiving suspicious reports in the AML /CFT field, and in taking necessary action and measures in coordinating with the concerned stakeholders in Zambia.

The FIC, through its financial analysis tools and close cooperation with the various supervisory authorities and law enforcement agencies, has actively followed up financial transactions exposed to economic crimes.

In the context of creating the appropriate environment for combating money laundering and terrorism financing, the FIC has worked to establish a wide circle of privileged relations with compliance officers of financial and non-financial institutions and supervisory authorities.

The FIC also extended its efforts by widening its relationships with the international financial intelligence units and Government institutions by signing various Memorandum of Understanding (MoUs) to enhance cooperation in exchanging information.

It is worth mentioning that the success of the FIC is based primarily on the support and cooperation received from various stakeholders, including the Government of the Republic of Zambia. In this regard, the Government of Zambia procured new office premises for the FIC in the year 2014.

It is my honour and privilege to present to you the FIC 2014 AML/CFT trends report.

Mary. C. Sikazwe (Mrs.)

**Director & Chief Executive Officer**



## **1.0 BACKGROUND**

The FIC is the central national agency for receiving, requesting, analysing and disseminating intelligence reports relating to suspicious financial transactions, bordering on Money Laundering (ML), Terrorist Financing (TF) and other serious crimes.

The Centre was set up in 2010 following the enactment of the Financial Intelligence Centre Act, No. 46 of 2010 (the Act) and became operational in November, 2013. The Centre started receiving suspicious transactions and spontaneous disclosure reports, in November 2013.

### **1.1 FIC Mandate**

Section 5 of the Act provides that the Centre shall be the sole designated agency responsible for the receipt, requesting, analysing and disseminating of the disclosure of suspicious transaction reports. The core function of the Centre is to receive reports of financial transactions from reporting entities, analyse them, and disseminate analysed information to Law Enforcement Agencies (LEAs) and other foreign designated authorities.

### **1.2 Synopsis**

This report is the first to be issued by the Centre on ML and TF techniques. The aim is to assist AML/CFT stakeholders to better understand the nature of existing and emerging ML and TF threats and pursue effective strategies to address those threats. Typology studies such as this assist stakeholders to implement effective strategies to investigate and prosecute ML and TF offences, as well as design and implement effective preventative measures. In light of the foregoing, the Centre is one of the agencies responsible for protecting the integrity of the financial system and

contributes to the administration of justice through its expertise in countering money laundering and the financing of terrorism.

The case studies within this report highlight the value of reporting suspicious financial transactions and other serious crimes. The case studies demonstrate how following the money trail is an effective way of detecting the activities of organised crime syndicates. The cases also highlight the value of a whole-of-government approach to combating organised crime. They detail successes achieved through the Centre, regulatory and law enforcement agencies working together and sharing intelligence information bordering on criminal activities. The report covers the period 1 January to 31 December 2014.

## **2.0 STATISTICS**

### **2.1 Number of Suspicious transaction reports received**

The Centre received 487 Suspicious Transaction Reports during 2014. We noted that 94% of STRs emanated from the banking sector and 6% represented other sectors.

### **2.2 Nature of Suspicions Reported**

The dominant grounds of suspicion during the year were:

- I. Large or unusual cash deposit –50%
- II. Activity inconsistent with customer profile – 14%
- III. Large or un usual inward and outward remittance - 14%

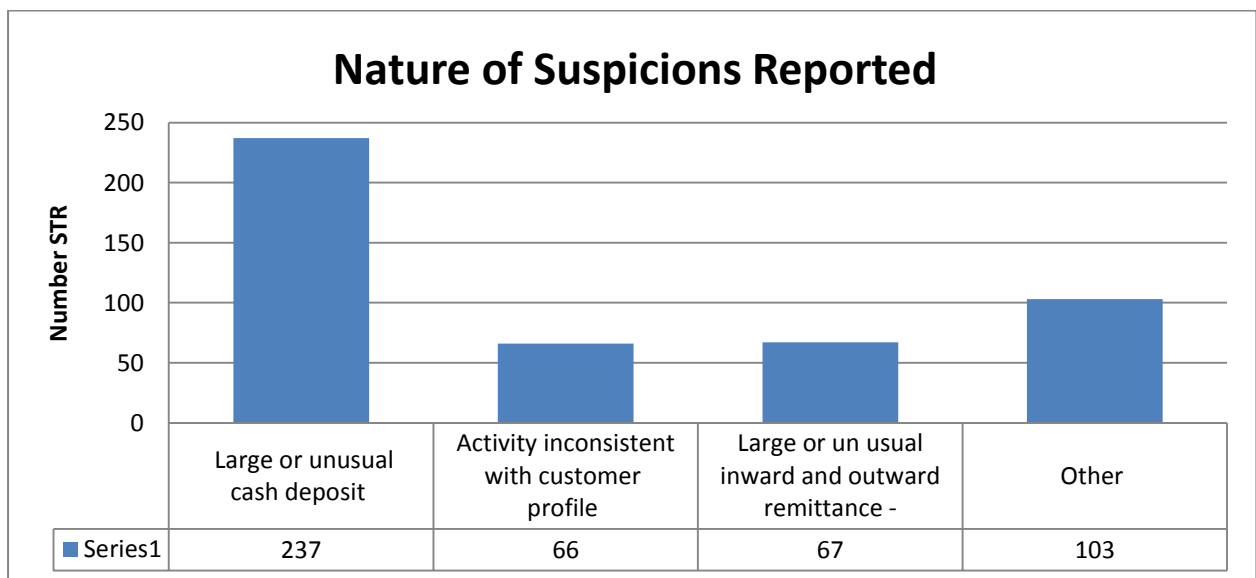
Zambia is largely a cash economy. The informal sector makes a significant part of the local economy. Transactions in this sector are largely cash based. However, the volume of the cash deposits do not always match the declared nature of business, suggesting

illicit sources of cash are finding their way into the banking system through cash deposits.

There is widespread use of personal accounts to route funds from business in order to evade tax. These funds are then remitted out of the country. It may be worthwhile, to consider criminalising the use of personal accounts for business purposes. Further, it may be necessary for the country to consider thresholds for businesses to prepare financial statements with attestation of some form from Accountants. This may assist the country begin to understand what may be happening in such business concerns.

The Centre will in 2015 introduce a cash transaction threshold. This shall compel reporting entities to report cash transactions above a certain limit as provided in the Act. In addition more institutions shall be designated as reporting entities for this purpose.

We present on the next page a graphical representation of the reported suspicions.



We provide as appendix 1 all the suspicions reported by type.

### 3.0 TREND ANALYSIS

The majority of STRs processed involve Retail, Construction and the Mining sectors. The following suspected crimes were identified as most prevalent:

- a. Illicit flow of funds
- b. Tax evasion
- c. Procurement fraud
- d. Bribery and Corruption
- e. Accounting fraud
- f. Cybercrime
- g. Money laundering

#### 3.1 Tax Evasion

Tax evasion as a predicate offence has been committed in various ways. They include false accounting, group company loans, use of personal accounts for business, transfer pricing and under valuation of exports. The precious stones industry is a case in point that will need more transparency in the sales and accounting to avoid the instance of under valuation.

- (i) The highest number of suspected offences relate to tax crimes.
- (ii) Perpetrators include both small and medium size entities to very large multi-national corporations.
- (iii) The large multi-national corporations are in the mining sector.

3.1.1 While focus is on the mines, a pattern is emerging that the entities doing business with the mines are also involved either:

- (i) on their own account; or
- (ii) aiding the mines with repatriation of value.



3.1.2 The list of methods the companies are using to evade payment of taxes established so far are as follows:

**3.1.3 Falsification of importation invoices-** Money laundering through the over- and under-invoicing of goods and services, which is one of the oldest methods of fraudulently transferring value across borders, remains a common practice today in our country. The key element of this technique is the misrepresentation of the price of the good or service in order to transfer additional value between the importer and exporter. By invoicing the good or service at a price below the “fair market” price, the exporter is able to transfer value to the importer, as the payment for the good or service will be lower than the value that the importer receives when it is sold on the open market. Alternatively, by invoicing the good or service at a price above the fair market price, the exporter is able to receive value from the importer, as the payment for the good or service is higher than the value that the importer will receive when it is sold on the open market. This ultimately impacts on the tax collected by the revenue authority.

**3.1.4 Foreign Loans /offshore centres –** Borrowing money does not make one rich and paying debts does not make one poor. Loans therefore are primarily of interest for tax purposes where related parties are involved, it leads to questions about the shifting of profits, limiting of the interest deductibility and the placement of informal

capital. This overall has a negative effect on the tax paid.

**3.1.5 Transfer pricing-** Transfer pricing is the setting of prices for transfers within the multinational enterprise (MNE). While transfer prices may be set for purely internal reasons, there are often strong external motivations to engage in transfer price manipulation (over/under invoicing) Insights from the fraud triangle (opportunity, pressure, rationalization) can explain why abusive TPM occurs and help design policy recommendations to reduce abusive TPM. The ulterior motives are to avoid or evade tax payments.

**3.1.6 Falsified financial statements** – this is an authorized alteration in company books to create a false impression of poor performance when in fact not.

**3.1.7 Unregistered Businesses** – these are instances where businesses operate without being registered with the Revenue Authority or PACRA.

### **3.2 Procurement fraud**

The Centre processed cases of suspected corruption in procurement. These cases were in Government contracts and foreign missions in Zambia. We present an illustration at page 11 through a case study.

### **3.3 Irregular Immigration Status**

Due to the country's geographical positioning, Zambia has for some time been a transit point for illegal migration. However, the recent surge in economic activity has now seen the country also become a recipient of illegal migration.

- (i) The huge investment in the mining sector has attracted labour from outside Zambia engaged either by the mines or contractors to the mines.
- (ii) A significant portion of this labour is from Asia and South America.
- (iii) Not all the labour hired is skilled and therefore some have difficulty obtaining work permits. Hence, some are in Zambia on visitors permit and subsequently obtain work permits in unclear circumstances.
- (iv) Some continue to work on a visitors permit and keep on extending them as they expire. This category of workers have no bank accounts and transfer funds to their home countries using accounts of their compatriots.
- (v) Some of their emoluments are not taxed. The remuneration is paid into their accounts in some countries. We have expatriates in Zambia that are paid officially as little as K3,000.00

#### **4.0 EMERGING, DECLINING AND CONTINUING TRENDS IN STRS**

##### **4.1 Emerging Trends**

**4.1.1 Use of personal account for business transactions to evade tax is pervasive.** Company funds transferred to personal accounts. This trend suggests lapses in the level of ongoing customer due diligence in banks. A customer that has declared monthly income of K10, 000.00 within months of a relationship with a bank can deposit K1 million, without red flags being raised.

##### **4.1.2 Use of bank accounts to externalize funds**

We have noted a trend whereby businesses and individuals are borrowing funds from jurisdictions that are known as tax havens from obscure institutions. The cost of borrowing is

normally high as a way to repatriate any profits made in the country. It is difficult to authenticate the loans contracted because of the opaque nature of jurisdictions in which the liabilities are contracted.

## **4.2 Declining Trends**

### **4.2.1 Cheque fraud**

We noted only two cases of cheque fraud.

## **4.3 Continuing Trends**

- i. False declaration of income
- ii. Substantial inter-account transfers between related accounts either controlled by self or through associates without any economic rationale
- iii. Frequent cash transactions of value just under the reporting threshold. Cash transactions spilt across accounts to avoid reporting
- iv. Large value of cash and cheques deposits in bank account followed by immediate cash withdrawals.
- v. Accounts used for providing fictitious purchase bills mostly abroad
- vi. Name of remitter/ beneficiary matching with watch lists
- vii. Withdrawal of large foreign remittance in cash without any valid explanation
- viii. Splitting of inward foreign remittances to collect funds in cash in an apparent attempt to avoid fund trail
- ix. The mining sector has presented the most significant challenge in terms of possible evasion of taxes.
- x. The use of related parties in the procurement process and the use of related commodities trading companies to overprice imports and under-price exports remains a challenge.

## **5.0 OUTLOOK AND FUTURE**

### **5.1 Cash Courier**

We noted a significant number of cash deposit reports. FATF Special Recommendation IX (SR IX) requires jurisdictions to implement measures to detect and prevent the physical cross-border transportation of currency and bearer negotiable instruments, which is one of the main methods used to move illicit funds, launder money and finance terrorism. We are working with other stakeholders to ensure thresholds are prescribed and more entities are designated for purposes of the reports.

### **5.2 Enhanced Information exchange with Government Ministries**

We have signed Memoranda of Understanding (MoUs) with various Government Institutions to enhance the exchange of information. Manual systems in some Government entities delay the retrieval of information and could compromise security in the event information is required urgently. The manual systems also deprive other Government entities from using the same information for other purposes.

Computerisation of Government systems will enhance transparency and efficiency with which information is retrieved.

### **5.3 Capacity Building**

The Centre is continuously building capacity to ensure it effectively handles its operations.

## 6.0 CASE STUDIES

As stated, the case studies highlight the value of industry's reporting of financial transactions and suspicious matters to the FIC. We present two actual cases of reports handled.

### 6.1 CASE STUDY I

#### 6.1.1 Tax evasion case study in the mining sector

The company M, incorporated in Zambia held an account which was credited with significant dollar amounts. This account received various international transfers from country X by order of a parent company to one of the mines in Zambia. Subsequently the money was transferred to various accounts to a country Z in East Africa. It was later noted that shareholders of company M had strong links with the recipients of the funds in country Z in East Africa. The amount involved is about USD 60 million.

The Centre's analysis revealed the following elements:

- Company M's registered business was agriculture, forestry, construction and fishing. However, it was noted that the company's major operation was in logistics management for mining companies. Company M was incorporated by two foreigners from country Z in East Africa. The suspicious transactions on the company's account commenced shortly after it was established.
- Suspected transfer pricing was taking place between the mine, the parent company and the logistics company. The gap between the market price and the non-arms length price was USD 300/ tonne.
- Company M was not tax compliant.
- Additional information revealed that one of the recipients of the funds in Zambia worked for a law

enforcement agency. Both nationals were given directorship roles in the company and had since established their own companies which have now been subcontracted for security and clearance roles respectively.

- Furthermore, the accounts of the 2 Zambian nationals were found to have operated above their declared thresholds. Information from the bank showed that the two nationals accounts were credited with substantial cash deposits and transfers from Company M. This money was mostly withdrawn in cash.

These elements seemed to indicate that the shareholders in company M played an active role in the illicit flow of funds. This case has been handed over to Law Enforcement Agencies for further investigation and prosecution of tax evasion and money laundering offices. We estimate the Government may have lost in excess of USD 15 million in tax revenues.

**Possible Offences:** Tax evasion and money laundering

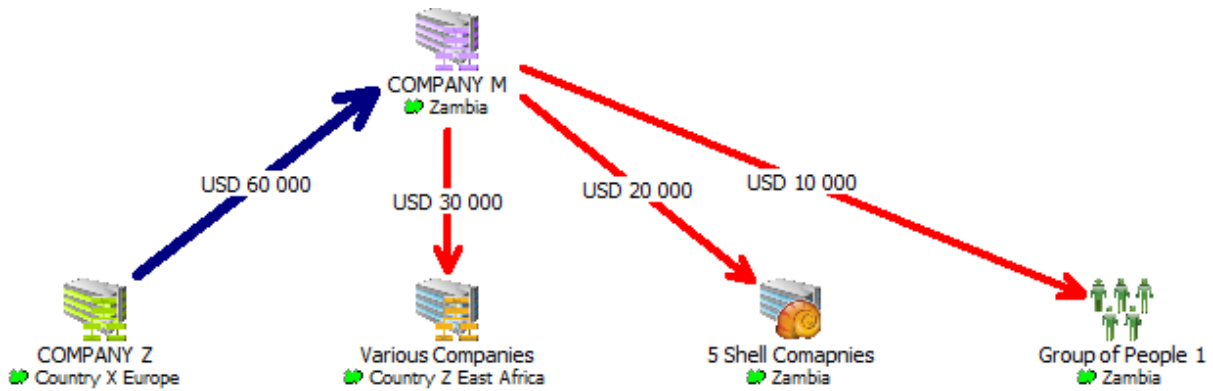
**Customer:** Corporations

**Industry :** Mining

**Jurisdiction:** Zambia

**Indicators:** Illicit funds transfers, concealment of sources of funds

### Case Study 1 Diagram – Illustration of Funds Flow



## 6.2 CASE STUDY 2

### 6.2.1 Corruption in the Construction Industry

Government Ministry 'B' invited bids for the construction of a training Institute in Town Y. The scope of works involved the construction of classrooms, hostels, and staff houses. Of the 23 bids received, Company 'Z' was awarded a K20 million contract which was to run for 180 weeks. Company Z was later paid K5 million by Ministry 'X' as initial instalment. The Centre received an STR alleging that Company 'Z' was fraudulently awarded a contract.

The Centre`s analysis revealed the following elements:

- Company 'Z' was not registered as a limited company by shares under the Companies Act Chapter 388 of the Laws of Zambia at time of bidding. It was noted that the subject company was registered under the Business Association Act Chapter 389 of the laws of Zambia as a sole trader. The bidding instructions were that only limited companies were to bid for the tender.
- Company "Z" had no tax clearance. The company was not complaint for tax purposes.



- We established that company “Z” had a longer completion period contrasted with other bidders. “Z” had a completion period of 104 Weeks at a cost of ZMW 17 Million and company “X” had a completion period of 54 weeks at a cost of ZMW 12 million. The evaluators still proceeded and gave the contract to company “Z”
- Evaluators from a Government ministry who were charged with the responsibility to conduct an evaluation of the bids lowered the value of company “Z ” by ZMW 3 million to ensure it succeeded in the bids.
- Evaluator “B” on the panel received a gratification of ZMW 250,000.00
- A physical site visit and inspection at the construction site reviewed that the project/construction site had been abandoned despite the payment of K 5 Million having been disbursed.

These elements seemed to indicate that the evaluators and Company “Z” proprietor played an active role in tender process.

This case was handed over to Law Enforcement Agencies for further investigation and prosecution. We estimate the Government may have lost in excess of ZMW 7 million.

**Possible Offences:** Corruption and Money Laundering

**Customer:** Corporations

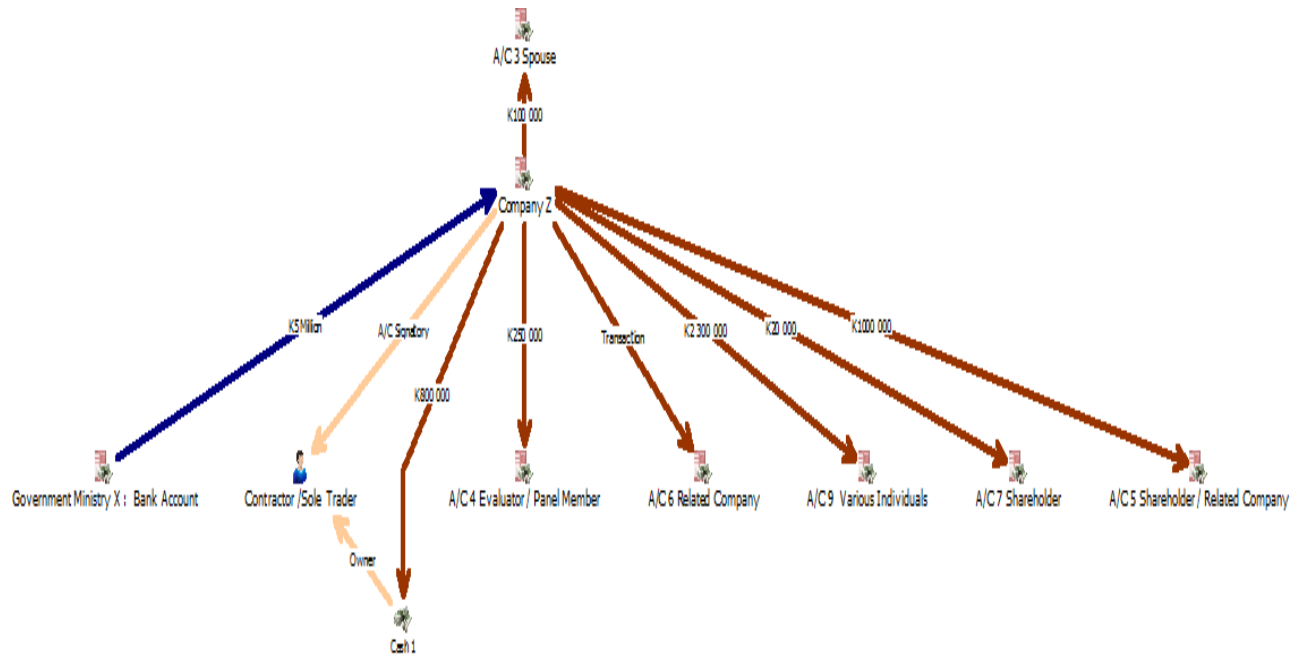
**Industry :** Construction

**Jurisdiction:** Zambia

**Indicators:** Bribery, fraud, illicit flow of funds  
concealment

of sources of funds.

**Case Study 2 Diagram – Illustration of Funds Flow**



## Appendix I

### Nature of Suspicion reported

Reason for Suspicion	2014	Percentage
Person – Suspicious Behaviour	0	0
Irregular or unusual international banking activity	2	0.4
Large or unusual cash deposit	237	50.4
Activity inconsistent with customer profile	66	14
Large or unusual inward remittance	67	14.1
Unusually large foreign currency transaction	3	0.6
Country/jurisdiction risk	1	0.2
False name/identity	0	0
Counterfeit currency	0	0
Fraud	2	0.4
Avoiding reporting obligations	4	0.8
Known/suspected criminal/organization	0	0
Unusual business practices	6	1.2
Many third parties making deposits into the account	4	0.8
Watch listed individual/organization	0	0
Phishing (Electronic Fraud)	0	0
ATM fraud	1	0.2
Or inactive account	2	0.4
Large or unusual cash withdrawals	0	0
Corporate/Investment fraud	0	0
Large or unusual outward remittance	23	4.9
Credit Card fraud	0	0
Credit/loan facility fraud	6	1.3
Currency not declared at border	0	0
Immigration related issue	2	0.4
Internet fraud	0	0
National Security concern	0	0
Unauthorized Transaction	0	0
Unusual Financial Instrument	0	0
Unusual Gambling	0	0
Advance fee Scam	0	0
tax evasion	5	1
transfer between accounts	1	0.2
Sudden activity on dormant accounts	2	0.4
Cheque deposits	39	8.3
Totals	473	100%