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MONEYVAL

Typology research

Money laundering through private pension funds and the insurance sector - Red flags and indicators [1]

[1] Adopted by MONEYVAL at its 32nd Plenary Meeting (Strasbourg, 15-18 March 2010).

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Money Laundering and Financing of Terrorism
Red Flags and Indicators for the Insurance and Private Pensions Sectors

I. INTRODUCTION

1. International standards in the fight against money laundering and financing of terrorism (including the 40+9 FATF Recommendations, the third European Union Directive, other regulations, policies, etc.) specify a range of obligations to which the financial and non-financial institutions are required to comply.

2. These requirements are required to be implemented by financial institutions and other designated businesses to prevent the entity from being exploited for the purposes of money laundering and financing of terrorism. In order to develop effective preventative controls and procedures it is important that financial institutions understand the nature of the risks and vulnerabilities that attach to their particular business.

3. The insurance industry has a number of features which enhances the risk of it being exploited for the purposes of a money laundering and financing of terrorism, in particular, its international nature and the savings and investments features of some of the products. Furthermore it is an industry that is used extensively by both natural persons as well as legal persons.

4. In recent years, the insurance and pensions sectors have experienced substantial and sustained growth in many countries in the MONEYVAL region. It is a particular feature of the MONEYVAL region that there has been significant growth in non-life insurance, which is not a regulated category in all of the countries concerned. In consequence of this, and following a risk analysis, some MONEYVAL countries, have made the choice to include this category on the list of obligors; the main reason frequently being the fact that currently the non-life market is bigger than the life sector.

5. The insurance sector is therefore an exposed business line and could be attractive to money launderers seeking to place funds into a financial product that will provide them with a reliable and clean return of funds invested. If a money launderer is able to move funds into an insurance product and to receive a payment made by an insurance company, then he will have given his funds the appearance of legitimacy.

6. Given the potential vulnerability of the insurance and pensions sectors, many MONEYVAL countries have developed guidelines and indicators. This report seeks to bring together a comprehensive list of red flags and indicators specifically for the insurance and private pensions sectors. These indicators are drawn from indicators developed by countries within the MONEYVAL region as well as other sources including international bodies such as the Financial Action Task Force (FATF) and the International Association of Insurance Supervisors (IAIS).

II. RED FLAGS AND INDICATORS

The suspicious indicators listed below are being provided here to give law enforcement, regulators and the private sector an overview of the types of activities that can be suspicious. This list is not exhaustive. Furthermore, it should be noted that some of these suspicious indicators and red flags may be not be applicable in all jurisdictions.

It is noted that the occurrence of one or more of these indicators/red flags may be a warning sign of unusual activity that may be indicative of money laundering (ML) / terrorist financing (TF) and/or the occurrence of an insurance specific designated offence. However, this does not necessarily mean that money laundering, terrorist financing or any other illicit activity is occurring. Further investigation should be conducted if any of these indicators/red flags are present during the course of a transaction or customer interaction.

This list of red flags and indicators is structured to cover:-

- Account opening
- Risk enhancing factors
- Payment and settlement of premiums
- Post-inception of policy
- Claims
- Special types of transaction and product

1. Account opening

A customer's profile, both financial and personal, represents the main benchmark against which the rationale for the transactions they perform or of the business relationships they entertain can be assessed. Some of the indicators that follow are applicable across all areas of the financial services industry whereas others are highly insurance sector-specific indicators. Clearly there may be innocent reasons why the policyholder acts in a way that initially raises suspicions, but it is for the insurer/intermediary to seek to verify such reasons.

General indicators

Due diligence

It is noted that due to the nature of some types of non-life insurance, it may be necessary to identify the policyholder and the nature of the underlying risk or asset insured.

- Customers who are reluctant to provide identifying information when purchasing a product, or who provide minimal or seemingly fictitious information and/or suspicious or fraudulent documents or ID.
- Delay in providing or failure to provide information to enable verification to be completed.
- Clients avoid direct contacts with employees, collaborators or the intermediary entity through frequent unjustified issue of mandates or powers of attorney.
- Applicant provides information that is difficult or expensive for the institution to verify.
- The applicant for insurance business uses a mailing address outside the jurisdiction and where during the verification process it is discovered that the home telephone has been disconnected.

- Reluctance to provide any information or provision of information in general or about the ownership of a risk which is difficult for the insurer to verify.
- Media reports of illegal activity.

Abnormal business requests

- Customers who seek or accept very unfavourable account/policy/contract provisions or riders.
- Any transaction involving an undisclosed party.
- Application for a policy from a potential customer in a distant place where a comparable policy could be provided "closer to home".
- Customers who show little concern for the investment performance of a product, but a great deal of concern about the early termination features of the product, including "free look" provisions.
- Insurance policies with premiums that exceed the client's apparent means.
- The applicant for insurance business appears to have policies with several institutions.
- Customer does not know what exactly he wants to insure yet is interested in all options, including the most irrelevant ones (e.g. Insurance against earthquakes in Poland)
- Insurance policies with values that appear to be inconsistent with the client's insurance needs.
- The requested insurance and/or proposed transactions have no apparent purpose, make no obvious economic sense and appear unrealistic, illegal or unethical.
- Purchase of a policy that does not meet the customer's needs, unrelated to his health or age (e.g. Disabled or elderly person and extreme sports).
- Use of common registration techniques for contracts that involve life insurance policies or change of names of registered persons for no obvious reason.
- Concluding multiple life insurance policies by a customer nominating different beneficiaries with no clear connection between them.
- The client conducts a transaction that results in a conspicuous increase of investment contributions.

Customer behaviour

- Insistence on speedy issue or service without the required paperwork or other requirements.
- Transactions in which customers unusually emphasise the necessity for secrecy, or they ask, force or bribe the insurance agent or intermediary not to report such transactions to the authorities.
- Customer acts in a hurry, does not analyse an offer, is not interested in charges and costs, chooses the most expensive option which may not necessarily be the most appropriate one.
- Appearance and abnormal behaviour of customer (e.g. Nervousness, lack of self-confidence, hesitation, clothing, etc.).
- Companion or other persons who influence and/or control customer's decisions and whose general behaviour appears suspicious.
- Attempts to corrupt an employee (an additional commission promised for loosening requirements and not paying attention to shortcomings of the client).
- The client suggests the duration of the life insurance contract to be shorter than the standard duration offered by the insurance company.

Corporate Customers

- Difficulties and delays in obtaining copies of accounts or other documents of incorporation, where required, about a new corporate/trust client.
- Significant and apparently unnecessary use of offshore accounts, companies/structures in circumstances where the client's needs do not support such economic requirements.
- The use of intermediate corporate vehicles or other structures that have no apparent commercial or other rationale or that unnecessarily increase the complexity of policy ownership or otherwise result in a lack of transparency. The use of such vehicles or structures, without an acceptable explanation, increases the risk.
- Insurance includes risks that are irrelevant to operating range (e.g. insurance against internet theft knowing that the customer has no access to the web).
- The insurance and premium is unreasonably high compared to annual turnover of the company.
- The company has new ownership and the background and appearance of the new owners (homeless people, etc.) does not harmonise with the company profile or the financial activities of the company suddenly change after the change of ownership.
- The financial indicators of the company concerned are significantly different from that of similar companies.
- The company is represented by a person (authorised to sign) whose appearance and skills obviously make him unsuitable for this, especially if such person is not an employee of the company.
- A company representative who is reluctant to reveal or is not fully aware of the nature of the company's underlying business.
- Transactions with insurance policies entered into on behalf of non-existent or fictitious companies.

Customer type

The fact that a customer falls into one of the categories listed below does not in itself mean that the object of the transaction is money laundering or the financing of terrorism. It does, however, indicate that extra care needs to be taken in accepting the customer and in subsequent monitoring of the performance of the policy.

- Customers that are legal persons whose structure makes it difficult to identify the ultimate beneficial owner or controlling interests.
- Charities and other "not for profit" organisations which are not subject to monitoring or supervision (especially those operating on a "cross-border" basis).
- "Gatekeepers" such as accountants, lawyers, or other professionals holding accounts, policies or contracts at an insurance company, acting on behalf of their clients, and where the insurance company places unreasonable reliance on the gatekeeper.
- Customers who are Politically Exposed Persons (PEPs).
- Customers where the beneficial owner of the contract is not known (e.g. certain trusts).
- Customers who are introduced through non face-to-face channels.
- A company is unreliable, involved in fraud and shady transactions, registered as an unreliable debtor.
- Where the policyholder is a known criminal, a relative or an associate of a known criminal. [2]

[2] It would be unfair to relate a transaction or a business relation to ML only because it is connected to someone with criminal precedents, but such connections can certainly be used as an indicator of risk. Clearly it is not always

2. Risk enhancing factors

Intermediaries

Both life and non-life insurance carriers rely heavily on intermediaries to introduce insurance business. This may mean that the insurer has to rely on the intermediary to conduct CDD and verification with the customer. Furthermore, intermediaries frequently control the cashflow between the insurer and the client. Although this is normal insurance business practice it does present opportunities for money laundering and the financing of terrorism.

- Reluctance by the intermediary to provide ownership details and other relevant company documentation.
- Business introduced by an agent/intermediary in an unregulated or loosely regulated jurisdiction or where organised criminal activities (e.g. Drug trafficking or terrorist activity) or corruption are prevalent.
- The overseas intermediary is based in a jurisdiction which has ineffective, poorly enforced or no money laundering legislation.
- Transactions involving third parties, whose involvement only becomes apparent at a later stage.
- Unnecessarily complex placing chains.
- Excessive commission paid to an intermediary or the involvement of an intermediary whose role appears superfluous.[3]
- Commission paid into a bank account in a different jurisdiction to the intermediary.
- Unusually high level of refunds and cancellations.
- Overpayments of premium with a request to repay the excess to a separate bank account.
- Resistance to audit of client money account.
- Results of an audit which reveals premium financing arrangements between policyholders and intermediaries, which may obscure source of funds or large unusual cash payments.
- Fraudulent documents presented by agent.

Geographical

Country risk may refer to the domicile of the policyholder, the location of the risk insured or the location of any intermediary involved in the transaction. In certain circumstances it may also relate to beneficiaries of life insurance policies.

Certain specialised insurance risks may only be possible to be insured in certain jurisdictions (e.g. specialist property and casualty risks at Lloyd's in London). Likewise, in order to spread a large risk an insurer may chose to reinsure in another jurisdiction. These are normal commercial transactions and should not of themselves give rise to a suspicion on money laundering or financing of terrorism.

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possible for insurers and intermediaries to gain relevant information, such as the personal criminal records of their own customers or of their relatives or associates, which are rightly deemed to be confidential. However, effective customer due diligence procedures and the use of differentiated sources of information may provide a deeper insight of both actual and potential customers. To this end, the implementation of channels for the exchange of information, to the extent permitted by legislation, within the insurance sector (or even wider) is desirable.

[3] Situations where intermediaries apply particularly high commission charges, i.e. in excess of the usual commission or fee charged for that type of product, to the policyholder are an indicator of enhanced ML risk. In such situations, the intermediary may be directly or indirectly involved in a ML operation, or simply knows that funds of dubious origin are involved in the transaction or since he can sense that the transactions featured a higher risk to himself, and thus demanded a higher than normal commission.

Insurance companies and intermediaries should take into account warnings issued by competent authorities about risks applicable to countries or geographic areas, including the specificity as to the particular risks posed. The fact that the insured risk is situated in or in transit to or through a country as set out below does not in itself mean that money laundering or terrorist financing is involved, nonetheless particular care should be exercised in taking on such business and a combination of other indicators could indicate that there is a suspicious transaction to report.

- Countries identified by FATF Statements as having weak AML/CFT regimes, and for which financial institutions should give special attention to business relationships and transactions.
- Countries or geographic areas subject to sanctions, embargoes, or statements of concern issued by international bodies such as the United Nations ("UN"), FATF, or governments. In addition, in some circumstances, countries subject to sanctions or measures similar to those issued by bodies such as the UN, but which may not be universally recognised, may be given credence by a life insurance company or intermediary because of the standing of the issuing body and the nature of the measures.
- Countries or geographic areas identified by credible sources as lacking appropriate AML/CFT laws, regulations and other measures.
- Countries or geographic areas identified by credible sources as providing funding or support for terrorist activities or that have designated terrorist organisations operating within them.
- Countries or geographic areas identified by credible sources as having significant levels of corruption, or other criminal activity.
- Countries or geographic areas where protection for customers "privacy" prevents the effective implementation of AML/CFT requirements and/or facilitates the framework for the establishment of shell-companies or the issuance of bearer shares.
- Cross border elements such as the insurer, the customer and the beneficiary of the contract being in separate jurisdictions (but see comments above).
- A request to insure goods, assets etc, in transit to or situated in countries where terrorism, the production of drugs, drug trafficking or an organised criminal activity may be prevalent or which are the subject of Financial Action Task Force warning notices or on their Non Cooperative Countries and Territories list or on the Transparency International Corruption Perceptions List.

Product

The following features may tend to increase the risk profile of a product:

- Allowance of withdrawals at any time with limited charges or fees.
- Acceptance to be used as collateral for a loan and/or written in a discretionary or other increased risk trust.
- Products that allow for assignment without the insurer being aware that the beneficiary of the contract has been changed until such time as a claim is made.
- Products that allow for high cash values.
- Products that accept high amount lump sum payments, coupled with liquidity features.
- Products with "free look" provisions, which allow for cancellation with full refund of premium within a defined "cooling-off" period.

3. Payment and settlement of premium

It is to be noted that many economies are still largely cash based for small transactions and elderly people are frequently more comfortable with cash than with other forms of payment. Therefore, the use of cash in itself does not necessarily mean that the transaction is linked to money laundering. This is particularly true with regard to savings products with small regular premium payments.

- Funds received from a country regarded as high risk (see under Geographical above).
- The receipt of premiums from offshore and/or lightly or unregulated financial intermediaries.
- The applicant for insurance business requests to make a lump sum payment by a wire transfer or with foreign currency.
- Premium paid from a foreign account in a different jurisdiction to the domicile or residence of the policyholder.
- Customers who use unusual payment methods, such as cash, cash equivalents (when such a usage of cash or cash equivalents is, in fact, unusual), endorsed money orders, cashier cheques or structured monetary instruments when the type of business transaction in question would normally be settled by cheques, credit or debit cards or other methods of payment.
- Attempts to use a third party cheque when purchasing a policy.
- Multiple sources of funds to pay premiums. [4]
- Acceptance of very high value or unlimited value payments or large volumes of lower value payments.
- Payment of a very large insurance premium which does not correspond to client's assets or income.
- Acceptance of frequent payments outside of a normal premium policy or payment schedule.
- An atypical incidence of pre-payment of insurance premiums.
- Insurance party requests a large purchase of a lump sum contract when the party usually makes small, regular payments.
- Money passing through a number of different persons and entities may introduce numerous layers to a transaction to create opacity and disguise the source of funds.
- Overpayment of premium and unwillingness to take it for a next premium instalment.
- One or several overpayments of the policy premiums followed by request that any reimbursement be paid to a third party.
- The client (as a natural person) performs payment of the insurance premium with funds from a legal person[5].
- Multiple payments of premium from different accounts that do not exceed a reportable threshold.

[4] It is unusual for funds used to pay policy premiums to originate from different sources, such as different banking institutions, even if all sources could eventually be referred to the policyholder himself. Accordingly, the purchase of the insurance policy in this manner may indicate operations at the layering or integration stage of ML.

[5] The exception to this would be circumstances where a legal person pays funds into an employee investment or pension policy as part of a "save as you earn" scheme.

4. Post-inception of policy

Customer behaviour

- Customers who transfer or assign the benefit of a product to an apparently unrelated third party.
- Policyholder substitutes the ultimate beneficiary with an apparently unrelated third party.
- Policyholder changes the designated beneficiaries without knowledge or consent of the insurer.
- Policyholder changes beneficiaries simply by signing an endorsement on the policy.
- Early termination of a product, especially at a loss, or where cash was tendered and/or the refund cheque is to a third party.
- The applicant for insurance business wants to borrow the maximum cash value of a single premium policy, soon after paying for the policy.
- Unusual viatical[6] sales.
- Frequent and unexplained movement of accounts/policies/contracts/funds to different insurance companies or other financial institutions.
- Using an insurer or insurance intermediary like a bank to move funds around.[7]

Refunds and cancellations

- Customers who seek early termination of a product (including during the "free look"/"cooling-off" period), especially at a cost to the customer.
- A number of policies taken out by the same insured for relatively small premiums (normally paid with cash) which are then quickly cancelled.
- Early surrender of investment type policies, especially where to do so defies economic logic.
- Cancellation of the policy and a request for the refund to be paid to a third party.
- Overpayment of premium with a request to pay the excess to a third party or in a foreign currency.
- Large and/or simultaneous requests of advance redemption of policies and/or their use to obtain loans, especially where this involves accepting disadvantageous conditions, or frequent partial cashing in of large single-premium policies.
- Request to cancel the insurance policy or using the right of exercising the exoneration clause in case of policies having high value premium without giving a valid explanation for so doing.
- Cancellation of a property casualty policy where the policyholder retains an interest in the underlying insured risks/assets.

[6] A viatical settlement is the sale of a life insurance policy by the policy owner before the policy matures. Such a sale, at a price discounted from the face amount of the policy but usually in excess of the premiums paid or current cash surrender value, provides the seller an immediate cash settlement. Generally, viatical settlements involve insured individuals with a shorter life expectancy.

[7] Insurers are now in the position of offering ever increasingly sophisticated products to their customers, increasingly competing with other parts of the financial sector. Many investment type life policies offer considerable flexibility in the making of additional premiums and early redemption. However where such products are used by a policyholder in a fashion similar to the way one would make use of a bank account, namely making additional premium payments and frequent partial redemptions, this is an indicator of possible ML. This risk is increased when transferring funds are received or paid to numerous accounts or to foreign jurisdictions (especially if a risky/non cooperative jurisdiction is involved or foreign exchange restrictions are in force in the receiving jurisdiction).

5. Claims

All insurance companies are vulnerable to insurance fraud and have mechanisms and procedures designed to identify and avoid fraudulent claims. The claims process can, however, be utilised to facilitate money laundering.

Nature of the Claim

- Apparently legitimate claims that occur with abnormal regularity e.g. Regular small claims within the premium limit from the same insured or intermediary.
- A change of ownership/assignment of the policy just prior to a loss occurring.
- Abnormal loss ratios for the class of risk bound under a binding authority, especially where the intermediary has claims settling authority (possible evidence of claims being fabricated and reported to underwriters, or under-reporting of claims where the intermediary is acting as unauthorised insurer, or even not paying claims).
- The customer withdraws a claim and gives up his rights when the insurance company requires additional documents.
- The client represents himself/herself as the authorised person of the claimant with no justified reasons (he/she is not a relative, guardian, professional adviser, etc.).

Settlement

- "Cash only[8]" reimbursement required.
- Claims paid to persons who are the subject of law enforcement or regulatory investigation.
- The customer readily accepts prompt payment of smaller than expected amount when the insurance company postpones payment of compensation or questions the amount of the claim.
- Customer unconditionally accepts an offer of a lower amount of reimbursement.
- Request for cash payments or issuance of several cheques in structured amounts under the reporting threshold, at maturity date.
- Reimbursement into a foreign account in currencies different to the original premium.

Payment to third parties

It is in the nature of insurance products that claims are frequently paid to persons other than the policyholder. This applies both to life (e.g. on the death of the policyholder) and to non-life (e.g. repairers, accident victims, etc.). It is nonetheless important to ensure that all payments are made to legitimate third parties.

- Claims requested to be paid to persons other than the insured or legitimate third parties.
- Claims requested to be paid to persons not naturally associated with the claim.
- Ceding of rights in favour of a third party (e.g. located in tax haven).

[8] See introduction under Payment and Settlement above.

6. Special types of transaction and product

Reinsurance

- Establishment of bogus insurers, which may be used to place the proceeds of crime or terrorist funds with legitimate reinsurers.
- Establishment of bogus reinsurers, which may be used to receive the proceeds of crime or terrorist funds from insurers or insurance intermediaries.
- Involvement of recently established insurance or reinsurance companies or companies whose background does not appear particularly transparent. [9]
- Treaty reinsurance policies with a level of claims at below the annual premium.
- Conclusion of reinsurance contracts with reinsurers in an off-shore centre with a reputation for low standards of supervision or in countries with high risk of money laundering or financing of terrorism.

Private pension schemes

The following indicators are specific to private pension schemes/voluntary pension funds (pension scheme). It should, however, be noted that many of the indicators set out above may also apply to pension schemes.

- Large cash sums deposited in Pension schemes by members of the scheme.
- Deposit of securities or other assets whose possession is not justified by the contractor's or policyholder's income-earning capacity and/or type of business payment into a capitalisation scheme.
- Transfer of assets from an unrelated third party into a capitalisation scheme.
- Insistence on depositing securities or other assets into a capitalisation scheme that would not normally be allowed by the scheme rules.
- Unrelated third party paying contributions cash on behalf of a member of a pension scheme.
- Unemployed person paying contributions into an employee pension scheme.
- Funds or other assets deposited into a pension scheme which are inconsistent with the profile of the policyholder.
- The type or volume of the transaction, which is untypical of the economic activity of the client and explanatory notes to transactions conducted by the client arise reasonable suspicion.
- The client performs a large number of identical transactions involving amounts immediately below or close to the threshold for reporting large transactions.
- The transaction is related to another transaction, which has already been reported to the FIU by a credit institution, credit union, investment brokerage company, investment management company, depository, organiser of a regulated market or pension fund.

[9] Whenever insurers or intermediaries have as their counterparts companies that are relatively new or have an opaque corporate and ownership structure, they should investigate more accurately their counterparts' background, with a view to ascertaining whether it is real companies they are dealing with and not fake undertakings or shell companies, which may be effectively used for ML purposes.