

- (a) As a measure of further liberalization of Exchange Control regulations, permission was granted to Registered Finance Companies (RFC's), Specialized Leasing Establishments (SLE's), Licensed Specialized Banks (LSB's) and selected supermarkets to conduct money changing business. Accordingly, new money changing licences were issued to 8 RFC, 1 SLE, 1 LSB and 2 supermarkets. Further, 11 Limited Liability Companies who fulfilled the existing eligibility criteria were permitted to engage in money changing business. Accordingly, altogether 23 new money changing licences were issued during the year 2011 bringing the total number of money changers to 82. Six money changers who were successful in purchasing foreign currency over US Dollars four million per annum were granted the permission to sell foreign currency.
- (b) 84 new companies were registered as freight forwarders, bringing the total number of freight forwarders to 429 at the end of 2011.
- (c) 46 new permits were issued to other restricted dealers, such as duty free shops, tourists' hotels/restaurants, gem and jewellery shops and travel agents in 2011. However, 30 permits were withdrawn due to their failure to comply with the terms and conditions of the permit and their secession from business, bringing the total number of such restricted dealers to 802.

### 9.6 Other activities

In continuation of efforts to promote worker remittances through the banking channels, a programme was conducted to encourage Authorized Dealers to formulate more convenient, efficient and less expensive mechanism for this purpose. Public awareness was enhanced on the relaxation of Exchange Control regulations. Authorized Dealers were also educated on such policy measures.

## 10. FINANCIAL INTELLIGENCE UNIT

In terms of the Financial Transactions Reporting Act (FTRA), No. 6 of 2006, the Financial Intelligence Unit (FIU) carried out its main functions that include collection and receipt of information on financial transactions for the purpose of detecting possible links to Money Laundering (ML), Terrorist Financing (TF) and other unlawful activities, investigations into suspicious financial transactions and dissemination of information and details of investigations to relevant regulatory and law enforcement authorities. The highlights of main functions of the FIU during 2011 are as follows.

### Collection of Information and Investigations

Licensed Commercial Banks (LCBs), Licensed Specialised Banks (LSBs), Registered Finance Companies (RFCs), Stock Brokering Firms (SBs) and Insurance Companies (ICs) continued to report to the FIU on cash transactions and electronic funds transfers (both local and foreign) of Rs. 1.0 million and above or its equivalent in foreign currencies through the FIU's on-line database management system, "LankaFIN". Accordingly, over 3.4 million of cash/fund

transfers and 539 suspicious transaction reports (STRs) were reported during the year 2011. After conducting preliminary investigations, 65 STRs were referred to the law enforcement agencies and regulatory authorities for further investigation. Based on the investigations conducted by the Criminal Investigations Department (CID), the Attorney General's Department has filed three indictments against money laundering offences and three indictments against terrorist financing offences as at 31.12.2011.

### Improvement in the Regulatory Framework

With the view to further strengthening the regulatory framework in line with the changes in international standards and best practices on Anti-Money Laundering (AML) and Countering the Financing of Terrorism (CFT), the FIU with the support of law making authorities arranged enactments of two Amendment Acts ; Prevention of Money Laundering Amendment Act No. 40 of 2011 and Convention on the Suppression of Terrorist Financing Amendment Act No. 41 of 2011 passed by the Parliament effective from 6th October 2011. The improvement on the legal framework is as follows:

### Convention on the Suppression of Terrorist Financing Amendment Act No. 41 of 2011:

- Applicability of terrorist financing law is widened by including citizens of Sri Lanka and non-citizens while present in Sri Lanka.
- The "Funds" is defined to include "assets of every kind whether it is tangible or intangible: movable or immovable" kept in Sri Lanka or outside Sri Lanka.
- Purview of the terrorist financing offence is widened to include financing of a terrorist (single terrorist) and / or for any terrorist act.
- Authority for police to freeze / suspend terrorist funds and properties relating to terrorist financing or activities before indictment.

### Prevention of Money Laundering Amendment Act No. 40 of 2011:

- Applicability of the law has been expanded to cover any person who has committed a Money Laundering offence while in Sri Lanka.
- Recovery of corresponding value of the properties related to a Money Laundering offence in the absence of properties derived/realized through Money Laundering.
- Coverage of unlawful activities relating to Money Laundering has been further expanded by lowering the punishment threshold from 7 years to 5 years.
- Foreign predicate offences are introduced as unlawful activities.

These amendments were aimed at improving the legal and regulatory system to combat money laundering and terrorist financing more effectively, keeping with the international standards recommended by Financial Action Task Force (FATF), the global AML/CFT standards and policy setter. Further, the FIU was in the process of finalizing the amendments to Financial Transaction Reporting Act, No. 6 of 2006 to strengthen the operations of the FIU.

The FIU also gazetted rules issued to financial institutions (LCBs and RFCs) in relation to Know-Your-Customer and Customer-Due-Diligence (KYC/CDD) requirements on 28th March 2011.

### Other Activities

#### i. Signing of Memorandums of Understanding:

As a mechanism to facilitate sharing of information and intelligence for the purpose of investigation and prosecution of suspicious transactions, the FIU signed four Memorandums of Understanding (MOUs) with Financial Transactions and Reports Analysis Centre of Canada, The Office for Money Laundering Prevention (OMLP) Slovenia, The Financial Intelligence Units of Fiji and South Africa. Accordingly, the total number of MOUs signed increased to 16 as at end of 2011.

#### ii. Institutional Capacity Building and Awareness Programmes:

In continued efforts to enhance the awareness on detecting, analyzing and reporting of money laundering and terrorist financing transactions, 28 awareness/training programmes were conducted during the year, accommodating more than 2,300 participants from LCBs, LSBs, RFCs, Police Department, educational and public institutions. Five such programmes were conducted with the assistance from the AUSTRAC; Australian FIU. Further, the FIU conducted two special programmes for judges in collaboration with High Court Judges' Association.

#### iii. International Relations:

- a). Egmont Group : The FIU obtained assistance from members of the Egmont Group (Association of the FIUs) to carry out investigations and collaborated with the member countries gathering evidence on their investigations. Total number of such instances that FIU exchanged information with foreign counterparty was recorded as 29 for the year 2011.
- b). Asia Pacific Group on Money Laundering: Sri Lanka, as a founder member of Asia Pacific Group on Money Laundering (APG), attended its 14th Annual Meeting held in India in June 2011 and the 14th Annual Typologies Workshop held in South Korea.

#### iv. Examinations

During the year 2011, FIU conducted four examinations of reporting institutions to assess their exposure to risk of ML and TF and non-compliances with the provision of FTRA and other rules and directions issued by the FIU.

was renamed the 'Financial Stability Studies Department' (FSSD) with effect from 15th November 2011, in order to refocus its objectives towards financial stability related studies and research. The main functions of the FSSD include conduct of macro-prudential surveillance, the preparation of the Financial System Stability Review (FSSR) and the facilitation of the meetings and functioning of the Financial System Stability Committee (FSSC) and the Financial System Stability Consultative Committee (FSSCC). A brief description of the main activities undertaken by the FSSD in 2011 is given below.

### 11.1 Macro-prudential surveillance

- a) The FSSD conducts macro-prudential surveillance to identify systemic risks to the financial sector and to assess its capacity to withstand such threats. This involves the analysis of global and domestic macroeconomic and financial market developments and the risk exposures of banking sector, other financial institutions and non-financial institutions. A comprehensive set of aggregate Financial Soundness Indicators is compiled on a periodic basis to monitor the health of key financial and non-financial institutions. The FSSD prepared regular Financial Sector Risk Assessment Reports for the FSSC.
- b) The FSSD computed a Financial Stress Indicator for Sri Lanka which is a composite indicator of the current level of stress in the various financial markets and the banking sector. The Financial Stress Indicator is compiled on a monthly basis.
- c) The FSSD also compiles the quarterly Banking Soundness Index which is an aggregate indicator of the soundness and stability of the banking sector. The FSSD also conducts stress tests based on the banking sector, based on sensitivity analysis on a quarterly basis, to ascertain the resilience of the sector to different types of risks such as credit risk, market risk and liquidity risk shocks. The FSSD has also initiated macro-financial stress tests by developing a credit risk model which examines the impact of certain macroeconomic variables on the asset quality of the banking sector.
- d) The FSSD also constructed a Corporate Sector Credit Worthiness Indicator to analyze the credit worthiness of the corporate sector in Sri Lanka by assessing the probability of default of companies listed on the Colombo Stock Exchange. Financial indicators representing profitability and leverage are the independent variables in the model.

### 11.2 Publications

The Financial System Stability Review (FSSR) 2010 was published in January 2011. The FSSR 2011 was prepared in the last quarter of 2011 and will be published in the first quarter of 2012. The FSSR 2011 containing six chapters and seven box articles provides an overall risk and stability assessment of the financial system, as well as an account of the major global and domestic macroeconomic and

## 11. FINANCIAL STABILITY STUDIES

The Financial System Stability Department (FSSD) was established in 2007 to assist the Central Bank of Sri Lanka (CBSL) in maintaining the financial system stability, which is one of the core objectives of the CBSL. The department