



Jersey Financial
Services Commission

GUIDANCE ON PROLIFERATION AND PROLIFERATION FINANCING

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PROLIFERATION

INTRODUCTION

This guidance has been issued in an effort to assist and raise awareness among those institutions regulated and supervised by the Commission of the risks of proliferation financing and to assist them in complying with existing legislation.

Definitions of the terms “proliferation” and “proliferation financing” are given below. All other definitions are contained in the [glossary section](#).

Having reviewed this guidance, regulated and supervised persons may wish to revisit the following areas of their business to consider whether proliferation financing is adequately addressed in the:

- provision of staff training;
- implementation of policies and procedures;
- risk assessments of customers and products – with special attention to trade finance and insurance; and
- application of enhanced due diligence in respect of higher-risk transactions and entities.

OVERVIEW

In summary, this guidance aims to address the following:

1. What is proliferation?
2. What is proliferation financing?
3. Why is the prevention and detection of proliferation and its financing important?
4. What are the difficulties faced with identifying proliferation and its financing?
5. What are the relevant international obligations in respect of proliferation and its financing?
6. Are there any proliferation and proliferation financing offences in Jersey?
7. What reporting obligations apply?
8. How can proliferation and its financing be targeted?
9. Why are export controls important?
10. What export controls exist in Jersey?
11. Why are financial measures important?
12. How should risk assessments of customers and products take into account proliferation and proliferation financing?
13. What verification can be sought regarding goods?
14. Should special attention be given to trade finance and insurance products?
15. Red Flag Indicators

1. WHAT IS PROLIFERATION?

1. Proliferation is the manufacture, acquisition, possession, development, export, transshipment, 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. It includes technology, goods, software, services or expertise.

2. WHAT IS PROLIFERATION FINANCING?

2. Proliferation financing is the act of providing funds or financial services which are used, in whole or in part, for the manufacture, acquisition, possession, development, export, transshipment, 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.

3. WHY IS THE PREVENTION AND DETECTION OF PROLIFERATION AND ITS FINANCING IMPORTANT?

3. Proliferation financing facilitates the movement and development of proliferation-sensitive goods. The movement and development of such items can contribute to global instability and may ultimately result in a loss of life, if proliferation-sensitive items are deployed.

4. WHAT ARE THE DIFFICULTIES FACED WITH IDENTIFYING PROLIFERATION AND ITS FINANCING?

4. There are a number of difficulties associated with identifying proliferation financing:
 - A growing trend in the purchase and sale of elementary components, as opposed to whole manufactured systems. The individual elementary components may also have legitimate uses (dual-use goods), making their identification for illegitimate purposes even more problematic.
 - Dual-use goods are difficult to identify, requiring specialist knowledge and can be described in common terms with many uses such as 'pumps'.
 - Networks through which proliferation-sensitive goods may be obtained tend to be complex. This, combined with the use of false documentation, allows for proliferation sensitive goods, the entities involved, the associated financial transactions and the ultimate end-user to avoid detection. Front companies, agents and other false end-users are often used to cover up the ultimate end-user.
 - Risk of proliferation financing is more likely to be present in cases where the source of funds is legal and the end-user of a type of goods involved is obscured, making identification of such activities difficult.

5. WHAT ARE THE RELEVANT INTERNATIONAL OBLIGATIONS IN RESPECT OF PROLIFERATION AND ITS FINANCING?

5. The UN Security Council Resolution 1540 – Non-Proliferation of Weapons of Mass Destruction ([“UNSCR 1540 \(2004\)”](#)) is concerned with the proliferation of nuclear, chemical and biological weapons, as well as their means of delivery. The general obligation on Member States is to prevent the activities described in UNSCR 1540 (2004), as below:

UNSCR 1540/2004

- “2. *Decides that all States, in accordance with their national procedures, shall adopt and enforce appropriate effective laws which prohibit any non-State actor to manufacture, acquire, possess, develop, transport, transfer or use nuclear, chemical or biological weapons and their means of delivery, in particular for terrorist purposes, as well as attempts to engage in any of the foregoing activities, participate in them as an accomplice, assist or finance them;*

3. *Decides also that all States shall take and enforce effective measures to establish domestic controls to prevent the proliferation of nuclear, chemical, or biological weapons and their means of delivery, including by establishing appropriate controls over related materials and to this end shall:*

(d) *Establish, develop, review and maintain appropriate effective national export and trans-shipment controls over such items, including appropriate laws and regulations to control export, transit, trans-shipment and re-export and controls on providing funds and services related to such export and trans-shipment such as financing, and transporting that would contribute to proliferation, as well as establishing end-user controls; and establishing and enforcing appropriate criminal or civil penalties for violations of such expert control laws and regulations.”*

6. Whilst the primary focus of UNSCR 1540 is the implementation of export controls, a number of jurisdictions have implemented targeted financial sanctions in order to meet the finance-related obligations contained in UNSCR 1540.

6. ARE THERE ANY PROLIFERATION AND PROLIFERATION FINANCING OFFENCES IN JERSEY?

7. There are three offences in Jersey law relevant to the development, production, acquisition, retention and transfer of nuclear, biological and chemical weapons. Those three offences apply in respect of acts performed outside Jersey by United Kingdom nationals resident in Jersey and bodies incorporated under the law of Jersey.

CRIME AND SECURITY (JERSEY) LAW 2003

8. Article 2(1) provides that it is an offence for a person to:
- knowingly cause a nuclear weapon explosion;
 - develop or produce, or participate in the development or production of, a nuclear weapon;
 - have a nuclear weapon in his or her possession;
 - participate in the transfer of a nuclear weapon; or
 - engage in military preparations, or in preparations of a military nature, intending to use or threaten to use, a nuclear weapon.
9. Under Article 2(5) a person guilty of an offence under Article 2 is liable to imprisonment for life.
10. Article 2(3) provides that for the purposes of paragraph (1)(b) a person participates in the development or production of a nuclear weapon if the person does any act which –
- facilitates the development by another person of the capability to produce or use a nuclear weapon; or
 - facilitates the making by another person of a nuclear weapon, knowing or having reason to believe that his or her act has (or will have) that effect.
11. In proceedings for an offence under Article 2(1)(b) it is a defence for the accused to show that he or she knew or believed that the object was a nuclear weapon but, as soon as reasonably practicable after the accused first knew or believed that fact, the accused took all reasonable steps to inform an officer of the States of Jersey Police Force of his or her knowledge or belief.

BIOLOGICAL WEAPONS ACT 1974 (JERSEY) ORDER 1974

12. Article 1 provides that:
- No person shall develop, produce, stockpile, acquire or retain –*
- any biological agent or toxin of a type and in a quantity that has no justification for prophylactic, protective or other peaceful purposes; or
 - any weapon, equipment or means of delivery designed to use biological agents or toxins for hostile purposes or in armed conflict.

13. In accordance with Article 1(3) any person contravening subparagraph (1) is guilty of an offence and liable to imprisonment for life.

CHEMICAL WEAPONS ACT 1996 (JERSEY) ORDER 1998

14. Article 2(1) provides that:

No person shall –

- a. use a chemical weapon;
- b. develop or produce a chemical weapon;
- c. have a chemical weapon in his possession;
- d. participate in the transfer of a chemical weapon; or
- e. engage in military preparations, or in preparations of a military nature, intending to use a chemical weapon.

15. Article 2(8) provides that a person contravening Article 2 is guilty of an offence and liable on conviction to imprisonment for life.

TERRORISM (JERSEY) LAW 2002

16. The following offences may also be relevant in relation to proliferation financing:

- Article 15 – Fund-raising for the purposes of terrorism;
- Article 16 – Possession of property for the purposes of terrorism;
- Article 17 – Entering or being concerned in an arrangement to fund terrorism;
- Article 18 – Money laundering terrorist property; and
- Article 23 – Failure to disclose by financial institutions.

7. WHAT REPORTING OBLIGATIONS APPLY?

17. The acquisition, possession, use, transfer, concealment or retention on behalf of another of assets that are the proceeds of the commission of an offence (including those set out in section 6 above) may result in the commission of a money laundering offence under Articles 32-34 of the [Proceeds of Crime \(Jersey\) Law 1999](#). Failing to report knowledge or suspicion that another person is engaged in money laundering is also an offence under Articles 34A and 34D of the Proceeds of Crime (Jersey) Law 1999.
18. The provision of funding for such purposes may also result in the commission of an offence under Article 2(1)(b) of the [Crime and Security \(Jersey\) Law 2003](#) (see section 6 above).
19. A defence is available in respect of the offences in Articles 32-34 of the [Proceeds of Crime \(Jersey\) Law 1999](#) and Article 2 of the [Crime and Security \(Jersey\) Law 2003](#) if a suspicious activity report is filed with the Joint Financial Crimes Unit within a reasonable time frame.
20. Institutions should also make a report to the Joint Financial Crimes Unit where they know or have reasonable grounds to suspect another person has committed an offence under Articles 15-18 of the [Terrorism \(Jersey\) Law 2002](#), so as not to commit an offence under Article 23.
21. In addition, the provision of funds, economic resources or specified goods to a person, subject to sanctions legislation as a result of being a proliferation concern, may result in the commission of an offence under specific sanctions legislation. Reports on potential sanctions breaches should be made to the Chief Minister's Department.

8. HOW CAN PROLIFERATION AND ITS FINANCING BE TARGETED?

22. There are two recognised mechanisms by which proliferation can be targeted; namely export controls and financial measures.

9. WHY ARE EXPORT CONTROLS IMPORTANT?

23. Proliferators act globally, masking their acquisitions as legitimate trade. Proliferators are known to exploit global commerce, for example by:
- operating in countries with weak export controls;
 - utilising free-trade zones where the obtaining and/or shipping of such goods are more likely to escape scrutiny; and
 - operating in countries with high volumes of international trade.
24. Export controls are thus the primary counter-proliferation safeguard, focussed on preventing the illegal transfer of proliferation-sensitive goods. Reports to the United Nations 1540 Committee suggest that only 80 out of 192 countries apply export controls, with varying degrees of implementation.¹

10. WHAT EXPORT CONTROLS EXIST IN JERSEY?

25. In Jersey the following legislation governs export controls:
- [Customs and Excise \(Import and Export Control\) \(Jersey\) Order 2006](#)
 - [Open General Export Licence \(includes provisions on dual use goods\)](#)
26. In addition, certain provisions of the United Kingdom's [Export Control Order 2008](#) apply to persons (natural and legal) carrying out activities in the United Kingdom, as well as "United Kingdom persons".
27. Section 11(1) of the [Export Control Act 2002](#) defines a "United Kingdom person" to mean a United Kingdom national, a Scottish partnership or a body incorporated under the law of any part of the United Kingdom.
28. Section 11(2) of the [Export Control Act 2002](#) provides that:
- (2) *For the purposes of the definition of "United Kingdom person" a United Kingdom national is an individual who is—*
- (a) *a British citizen, a British overseas territories citizen, a British National (Overseas) or a British Overseas citizen;*
 - (b) *a person who under the British Nationality Act 1981 (c. 61) is a British subject; or*
 - (c) *a British protected person within the meaning of that Act.*
29. For example, under Article 20 of the [Export Control Order 2008](#) persons carrying out activities in the United Kingdom and United Kingdom persons shall not directly or indirectly—
- a. *supply or deliver;*
 - b. *agree to supply or deliver; or*
 - c. *do any act calculated to promote the supply or delivery of any goods subject to trade controls from one third country to another third country that is an embargoed destination.*
30. Article 19 of the [Export Control Order 2008](#) creates an offence for providing technical assistance for WMD purposes, which is also applicable to United Kingdom persons. Both the offences in Articles 19 and 20 can be committed by United Kingdom persons, wherever they are in the world.
31. An "embargoed destination" is a country listed in Part 1 or 2 of Schedule 4 of the [Export Control Order 2008](#). Embargoed destinations include jurisdictions such as Iran, Armenia, Azerbaijan and Sudan. The list of jurisdictions in Parts 1 and 2 of Schedule 4 of the [Export Control Order 2008](#) may assist institutions in determining higher risk jurisdictions for the purposes of this guidance.

¹ Page 7, paragraph 16 <http://www.fatf-gafi.org/dataoecd/32/40/45049911.pdf>

11. WHY ARE FINANCIAL MEASURES IMPORTANT?

32. Financial measures act as a supplement to effective export controls, to address the financial activity associated with proliferation. Similar to international criminal networks, proliferation networks use the international financial system to carry out transactions and business deals. Institutions should be alert to the possibility that their customers may be engaging in, or facilitating, proliferation activities.
33. The Financial Action Task Force's [February 2010 Working Group Report](#) suggests there are three areas where institutions might have responsibilities in relation to proliferation financing, namely:
 - a. the risk assessment of customers and products;
 - b. enhanced due diligence on high-risk transactions and entities; and
 - c. special attention to trade finance and insurance products.

12. HOW SHOULD RISK ASSESSMENTS OF CUSTOMERS AND PRODUCTS TAKE INTO ACCOUNT PROLIFERATION AND PROLIFERATION FINANCING?

34. Introducing proliferation financing within current risk assessment practice should be proportionate, given the overall proliferation risk associated with the activities undertaken by the institution. For example, an institution operating internationally or with an international client base will generally assess a wider range of risks, including proliferation risks, compared to a smaller domestically focused institution.
35. The following risks may be relevant to formulating a proliferation focussed risk assessment:

COUNTRY/GEOGRAPHIC RISK

36. The most immediate indicator will be links to a country that is subject to sanctions imposing restrictions on the movement of military goods²: In addition, sanctions measures requiring specific action against proliferation have been applied in respect of Iran and North Korea.
37. Other indicators may be that a country:
 - presents an ongoing and substantial money laundering and terrorist financing risks or have strategic deficiencies in the fight against money laundering and the financing of terrorism, e.g. those identified by the FATF (and listed in Appendix D of the [Handbook for the Protection and Detection of Money Laundering and the Financing of Terrorism for Financial Services Businesses regulated under the Regulatory Laws](#));
 - is an “embargoed destination” listed in Part 1 or 2 of Schedule 4 of the UK’s [Export Control Order 2008](#);
 - has strong links (such as funding or other support) with terrorist activities, e.g.: those designated by the US Secretary of State as state sponsors of terrorism; and those physical areas identified by the US (in its annual report entitled Country Reports on Terrorism) as ungoverned, under-governed or ill-governed where terrorists are able to organise, plan, raise funds, communicate, recruit, train, transit and operate in relative security because of inadequate governance capability, political will, or both; or
 - has higher levels of organised crime linked to arms dealing.

CUSTOMER RISK

38. Specific categories of customer whose activities may indicate a higher risk are:
 - Those on [national lists concerning high risk entities](#). For example, the United Kingdom’s Iran End-Users List identifies over 100 entities that may potentially pose a proliferation concern.
 - Where a military or research body is connected with a higher-risk jurisdiction of proliferation concern.
 - Where a customer is involved in the supply, purchase or sale of dual-use, proliferation-sensitive or military goods.

² http://www.jerseyfsc.org/the_commission/sanctions/index.asp.

PRODUCT AND SERVICE RISKS

39. The following may suggest higher risks:
- delivery of services subject to sanctions e.g. correspondent banking services captured under Iranian sanctions measures;
 - project financing of sensitive industries in higher risk jurisdictions;
 - trade finance services, transactions and insurance products involving higher risk jurisdictions; or
 - delivery of high volumes of dual-use, proliferation-sensitive or military goods, particularly if to a higher risk country.
40. As well as risk factors, mitigating factors should also be considered. For example, whether a customer is aware of proliferation risks and has systems and processes to ensure its compliance with export control obligations and can provide copies of export control licences received.

ENHANCED DUE DILIGENCE ON HIGHER-RISK TRANSACTIONS AND ENTITIES

41. Under Article 15(1) of the [Money Laundering Order 2008](#) institutions must apply, on a risk-sensitive basis, enhanced customer due diligence measures in any situation which by its nature can present a higher risk of money laundering.
42. It is a matter for institutions to determine the enhanced due diligence measures to be applied.
43. [Lists compiled by national authorities](#) can be a useful resource, as they provide information on individuals who may pose a proliferation concern. In individual cases, where proliferation financing is a risk or concern, institutions may wish to consider whether issuing banks, applicants or beneficiaries of letters of credit, or freight companies and shipping lines moving the goods, appear on such lists.
44. Where a Jersey regulated entity provides services to a trading company or any vehicle that itself has links to higher risk countries, from a proliferation perspective, development of a strategy will assist in responding to any proliferation risks. Such a strategy may call for systems to be put in place to monitor trading activities.

13. WHAT VERIFICATION CAN BE SOUGHT REGARDING GOODS?

45. Identifying whether a particular good is a dual-use good or otherwise a proliferation concern, is acknowledged to be difficult. Thus, in higher risk scenarios where the customer is importing or exporting goods, institutions should be alert to the need to mitigate against inadvertent proliferation financing. This can be achieved by asking the customer for the following:
- valid export licences; or
 - licence not required letters that are less than three months old.
46. If a customer is unable to provide the information referred to above, then an alternative is to ask that the customer provide evidence, by reference to export control requirements in the relevant jurisdiction, that the goods being exported do not require a licence.

14. SHOULD SPECIAL ATTENTION BE GIVEN TO TRADE FINANCE AND INSURANCE PRODUCTS?

47. A fairly significant proportion of proliferation activities will use trade finance as a vehicle. Thus special attention should be given to certain trade finance and insurance activities, for example:
- direct loans or general credit facility to facilitate export transactions;
 - purchase of promissory notes or bills of exchange issued by foreign buyers to exporters for the purchase of goods and services, freeing up cash for the exporter;
 - factoring - the purchase or discounting of a foreign account receivable for cash at a discount from the face value;
 - provision of guarantees to or by financial institutions on behalf of exporters such as pre-shipment guarantees and performance guarantees; or

- provision of insurance against certain risks in the trading process.

15. RED FLAG INDICATORS

48. To assist with awareness of potential proliferation financing a list of red flag indicators are provided below.

CUSTOMER

- The customer is involved in the supply, sale, delivery or purchase of dual-use, proliferation-sensitive or military goods, particularly to higher risk jurisdictions.
- The customer or counter-party, or its address, is the same or similar to one of the parties found on publicly [available lists](#).
- The customer is a military or research body connected with a higher risk jurisdiction of proliferation concern.
- Customer activity does not match the business profile.
- Customer is vague, particularly about end user and end use, provides incomplete information or is resistant to providing additional information when sought.
- A new customer requests a letter of credit from a bank, whilst still awaiting approval of its account.
- Complicated structures to conceal involvement – use of layered letters of credit, front companies, intermediaries and brokers.

TRANSACTIONS/ORDERS

- The transaction concerns dual-use, proliferation-sensitive or military goods, whether licensable or not.
- The transaction involves an individual or entity in a foreign country of proliferation concern.
- Transaction demonstrates a link between representatives of companies exchanging goods e.g. same owners or management, in order to evade scrutiny of the goods exchanged.
- Transaction involves the shipment of goods inconsistent with normal geographic trade patterns i.e. where the country involved does not normally export or import the types of goods concerned.
- Order for goods is placed by firms or individuals from foreign countries, other than the country of the stated end-user.

JURISDICTION

- Countries with weak financial safeguards and which are actively engaged with a sanctioned country.
- A presence of an industry that produces dual-use goods, proliferation-sensitive items or military goods.
- Deliberate insertion of extra links into the supply chain e.g. diverting shipments through a third country.

OTHER

- Final destination or end-use unclear.
- Project financing and complex loans, where there is a presence of other objective factors such as an identified end-user.
- Declared value of shipment under-valued in relation to shipping cost.
- Inconsistencies in information contained in trade documents and financial flows e.g. names, addresses, final destination.
- Use of fraudulent documents and identities e.g. false end-use certificates and forged export or re-export certificates.

- Use of facilitators to ensure the transfer of goods avoids inspection.
- Innocuous commercial wording on customs declaration/export licence e.g. pump (without further explanation of purpose/use).
- A freight forwarding firm being listed as the product's final destination.
- Wire instructions or payment from or due to entities not identified on the original letter of credit or other documentation.
- Pattern of wire transfer activity that shows unusual patterns or has no apparent purpose.