HELPING TO DRIVE FINANCIAL CRIME OUT OF THE UK ECONOMY

HOW DATA CAN TRANSFORM YOUR APPROACH TO DETECTING AND PREVENTING FINANCIAL CRIME

Over the past year, we have conducted extensive market research to put together a picture of the characteristics of money launderers and fraudsters and how they use UK firms to carry out their crimes. We've then assessed the data available in the UK to detect these characteristics, a process which has uncovered some very questionable looking businesses.

HOW TO RECOGNISE A MONEY LAUNDERER

Our research identified a number of key characteristics shared by those in the money laundering business:

They often use formation agents and leverage shell companies. These companies can be bought around the world and benefit from some trading history. Monitoring companies born from formation agents for a change in ownership is critical for understanding their activation point – the date after which criminal activity is most likely to begin.

The Ultimate Beneficial Owners are difficult to identify as they hide behind complex corporate structures often spanning multiple jurisdictions, especially tax havens that promise secrecy.

Their registered office address is commonly a home address, serviced office or mailbox. This is particularly suspicious where the company has a large turnover. Businesses where the registered office has defaulted to a Companies House-registered office address in Cardiff are also dubious. This address is common for residential addresses that have been stolen and where the theft has been reported to Companies House.

If you see the director linked to hundreds of companies, or a residential address being used as a registered office with links to hundreds of companies, these are both red flags.

If the directors are not based in the UK or are spread across multiple jurisdictions, this can be a concern. In addition, watch out for business owners or companies associated with high-risk jurisdictions.

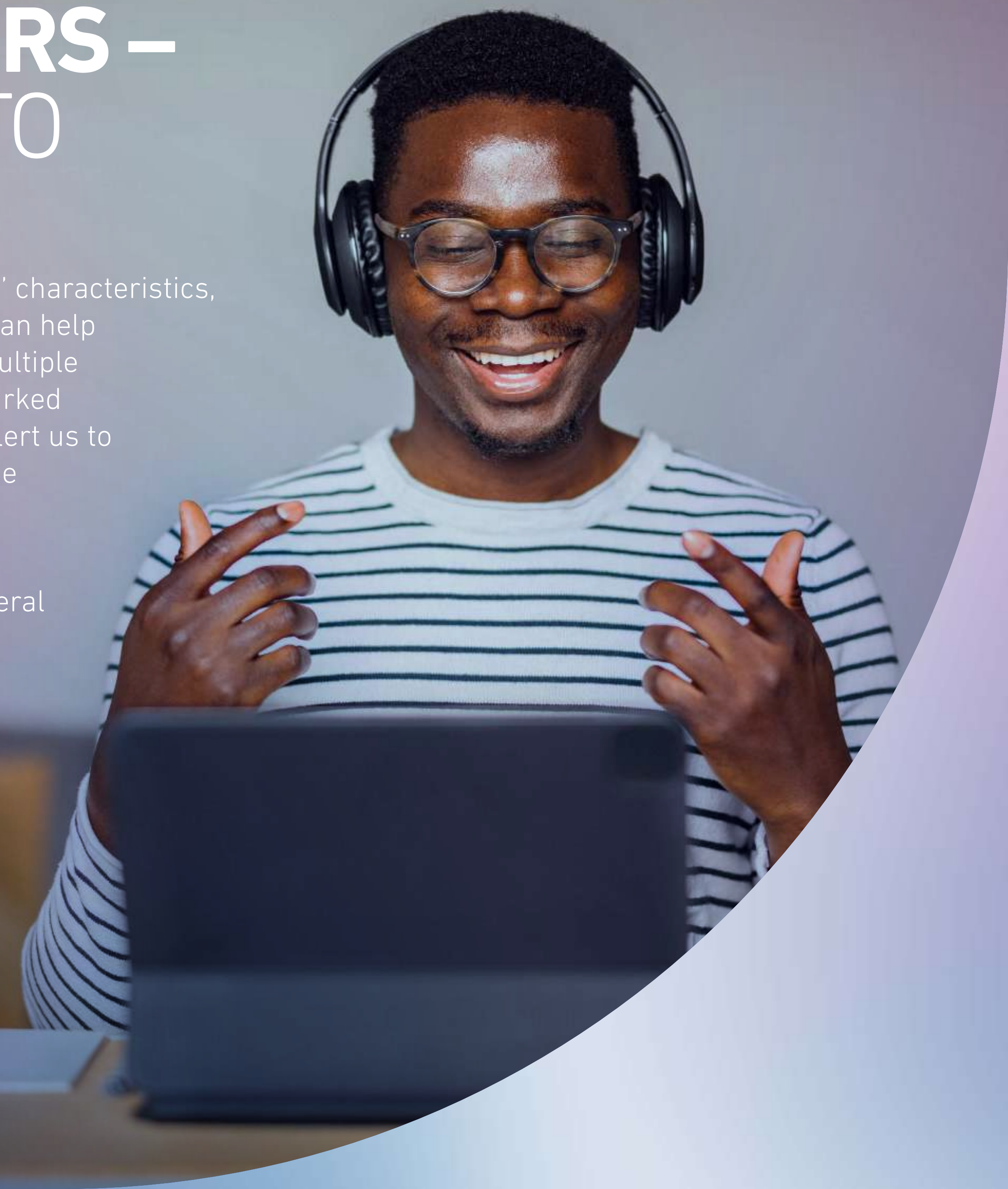
While you will be screening your customers for adverse media, a lack of online presence is equally concerning, especially if the company is presenting itself as large, old and established.

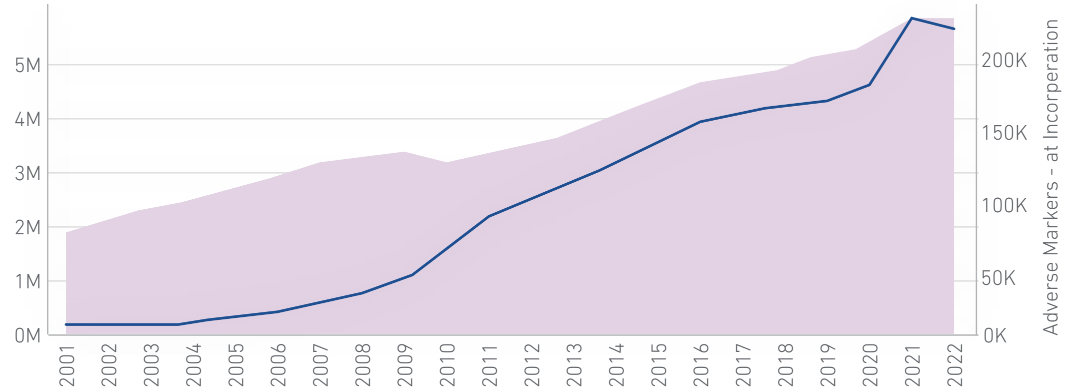
They lie! Fraudsters and money launderers will typically misrepresent themselves across multiple databases. Look for discrepancies in the way they present themselves across multiple sources. Experian has identified one such director who has more than 10 companies registered with Companies House, but where his country of residence is different for each business. Multi-sourced data corroboration is key for verifying your business customers.

ADVERSE MARKERS – WARNING SIGNS TO WATCH OUT FOR

Leveraging this understanding of money launderers' characteristics, we have catalogued over 50 adverse markers that can help businesses identify concerning behaviours. From multiple directors in different or high-risk jurisdictions to marked increases in cash inflow and outflow, the markers alert us to potentially suspicious activity. The more markers, the greater the likelihood of criminal activity.

We have recently completed some analysis on the adverse marker population, comparing it to the general business population.





The graph shown gives striking evidence of how adverse markers can flag questionable behaviour, even at a macro level. The shaded area represents the growth of the UK business universe between 2001 and 2022. The blue line illustrates the adverse marker population; those businesses exhibiting one or more adverse markers.

While we can see the adverse marker population is growing at a faster rate than the UK business universe, there is a particularly marked increase in growth from 2020 to 2021. At a time when the government was offering unprecedented support to businesses (due to Covid), and when it had been reported that fraud in government-backed schemes was rife, we see an exponential increase in the adverse marker population.

HOW TRANSACTION MONITORING CAN HELP

For banks around the world, transaction monitoring (TM) is critical for uncovering suspicious behaviour. When a business customer onboards, the bank will ask them about their expected annual transaction activity. This then forms a baseline against which the customer will be monitored.

The criminals, knowing this, will try to beat the TM systems. So what transaction characteristics do money launderers display?

They like to transact in round balances below set thresholds. For example, consumer transactions may come in at £9,900 or commercial transactions may come in at £990,000, conspicuously rounded at pound value with rarely any pennies. The commercial transaction value is much larger, which is why businesses are the preferred option for criminals looking to wash vast quantities of money. The small transaction monitoring threshold for consumers makes it difficult to launder high monetary values. The criminals, through industry research or by corrupting bank personnel, identify the transaction levels commonly monitored for, and the deposit values that won't automatically trigger an alert.

They usually transfer the money immediately out of the accounts and prefer not to leave high values in the accounts overnight. Money deposited in an account overnight and left for several days is more likely to be spotted and seized.

The inflows and outflows do not always match the business profile. It's important to establish what normal transaction activity looks like for each business profile by looking at a company's age, size and sector. If they sit outside the norm, this could be a sign of a money laundering business.

They like to use multiple bank accounts across multiple providers.

ADDRESSING FLAWS IN THE TM SYSTEM

The point about multiple bank accounts across multiple providers is an important one. Despite their sophistication, today's TM systems have one fatal weakness: they don't capture a true cross-industry view – and fixing this flaw presents a particular challenge. As the industry understands all too well, criminals tend to transfer money between a very high volume of accounts across multiple banks, aiming to obscure the origins of the funds and confuse even the most tenacious investigators.

Experian is looking to address this.

In March 2015, the Small Business Enterprise and Employment (SBEE) Act was passed, with the goal of stimulating the economy by increasing the flow of lending to small and medium-sized enterprises (SMEs).

The Act was designed to address one of the perceived barriers preventing SMEs from gaining access to the best finance options: the inequality of information available to banks of different sizes. While the established main banks held current account relationships with more than 90% of SMEs, with the data to match, other smaller lenders had little or no access to information about current account behaviour.

That all changed as a consequence of the SBEE Act. Now, Current Account Turnover (CATO) data is available via the rules of Mandatory Credit Data Sharing (MCDS) set out in the Act. The Act mandates the nine largest banks (by market share of SMEs in the UK and Ireland) to share with Experian the data they hold on their SME portfolios.

For the first time, we are able to leverage the valuable aggregate transaction data provided by the UK's largest banks to uncover previously hidden risks of financial crime.

IN MARCH 2015, THE SMALL BUSINESS ENTERPRISE AND EMPLOYMENT (SBEE) ACT WAS PASSED

CATO DATA – ENHANCING OUR ABILITY TO DETECT FINANCIAL CRIME

We can assess the total inflows and outflows for a business, drawing on CATO data from every current account it has opened across any of the major UK banks. So now, armed with a complete picture of a company's transaction behaviour across the entire banking industry, we can profile all businesses to establish precisely what account activity is normal for each one.

More importantly, we can now also identify deviations from that norm.

TM triggers are commonly assessed independently of other adverse markers. By looking at just one set of triggers and not assessing them holistically, valuable context can be missed, which either introduces higher false positive rates or, worse, misses the seriousness of the behaviour being exhibited. This is something we believe must still be addressed in the market.

TRUE FINANCIAL CRIME STORIES

By bringing our understanding of key money laundering characteristics and knowledge of adverse markers together with industry transaction data, Experian believes we can support the industry in its efforts to improve the detection of money launderers. Armed with adverse markers, combined with industry CATO data, we are able to quickly identify some very concerning-looking businesses. Here are some real-life examples found over the past year.

EXAMPLE 1 – MULTIPLE ADVERSE MARKERS

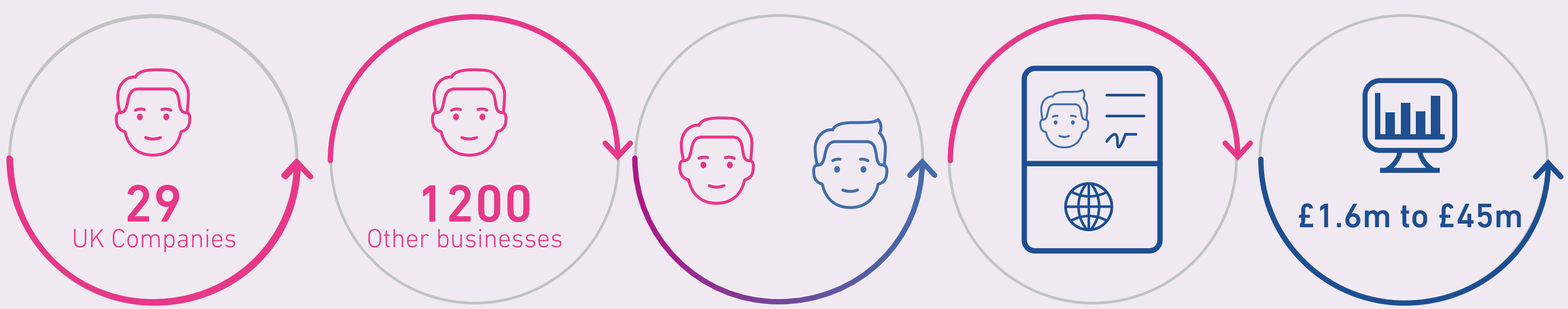
The example below shows a company born from a formation agent where the director is linked to a high volume of questionable firms. The director resigns and a new director from a high-risk jurisdiction is appointed.

Almost immediately following the appointment of the new director, inflows and outflows increase from £1.6m to over £45m. Experian has modelled the business's turnover at around £2m.

The inflows and outflows grow gradually month by month.

If a bank was looking at the transaction data in isolation, would the gradual increases have been spotted? Perhaps so but consider this added context: the firm was born from a formation agent with a questionable director linked to over 1,200 organisations, and the new appointed director was linked to a high-risk jurisdiction. This wealth of additional adverse information paints a much stronger picture of an extremely high-risk business.

True Finacial Crime Stories:



Mr X set up **29 UK companies** on the same day although did not reside in the UK

Mr X is also director of **1,200 other businesses**

Mr X resigns as director and is replaced by **Mr Y** who holds nationality within a high-risk third country

Mr Y then changes his nationality to British

Current account turnover increases from **£1.6m to £45m**

Such a vast increase in revenue in-flows and out-flows, almost as soon as the director's nationality changed, could be questioned.

But would this situation be picked up a bank's transaction monitoring, and would the context exist to cause grounds for suspicion?

EXAMPLE 2 – CAPITALISING ON AN INCREASED DEATH RATE

Money launderers are opportunistic. They are always looking for new ways to launder their ill-gotten gains. With the Covid pandemic, we sadly witnessed global increases in death rates.

The American Banker reported that criminals capitalised on this situation, using funeral directors to aid money launderers to wash their money at much higher levels, through a sector commonly considered to be low risk.

In one such case, Experian's adverse markers and aggregate transaction data identifies a funeral parlour that is six years old. When comparing the business to its peer group we observe some marked deviations from normal activity.

FIRSTLY, EXPERIAN'S ADVERSE MARKERS TRIGGER FIVE ALERTS:

01 Multi-jurisdiction directors

02 Conflicting nationalities

03 Conflicting country of residence

04 Conflicting date of birth

05 No Person of Significant Control

In the table above you will see five directors, however four of them display inconsistencies in where they are reported to be living. One even shows a discrepancy against their date of birth.

The cashflow flags have also triggered three alerts:

Credit Turnover
Standard Deviation Ratio:
4 x normal bahaviour

Debit Turnover
Standard Deviation Ratio:
2 x normal bahaviour

Maximum Balance
Standard Deviation Ratio:
5 x normal bahaviour

The company's inflows and outflows do not match the profile of the business, when assessing its age, size and sector.

XYZ Funerals Ltd.

Statement of comprehensive income for the year ended 31 december 2021

	2021 £	2020 £
Turnover	**11,456,914**	***7,664,579***
Cost of sales	(5,392,768)	*(5,068,682)*
Gross profit	**6,064,146**	***2,595,897***
Administrative expenses	(5,107,420)	*(1,131,523)*
Operating profit	**956,726**	***1,464,374***
interest receivable and similar income	(36,240)	*(36,629)*
Profit before taxation	**992,966**	***1,501,203***
Tax on profit	(184,576)	*(286,509)*
Profit for financial year	**808,390**	***1,214,694***

There were no recognised gain and losses for 2021 or 2020 other than those included in the Statement of Comprehensive income.

The notes pages 13 to 26 form part of these financial statements.

Business Profile

Age: 6

Sector: Funeral and related activities

Peer Group

Age: 5-9 years

Sector: Other Personal Service Activities

Expected turnover: £1m -£2.5m

Cashflow Flags

- Credit Turnover Standard Deviation Ratio: 4
- Debit Turnover Standard Deviation Ratio: 2
- Maximum Balance Standard Deviation Ratio: 5

Accounting Period	Credit Turnover	Debit Turnover	Average daily balance	# of Current Accounts
2017	1,253,441	1,309,511	48,600	1
2018	2,738,343	2,645,202	54,321	2
2019	6,535,760	5,929,063	260,237	2
2020	9,040,870	8,552,984	950,135	3
2021	20,137,267	20,444,536	2,013,567	3

The table above compares the turnover filed with Companies House on the left to the Experian turnover captured through the shared transaction data, CATO, obtained from three current accounts.

In 2020, the company files a turnover of £7.6m with Companies House against Experian's calculated £9m, and in 2021, the discrepancy grows considerably with Experian capturing £20m against the company's filed turnover of £11.4m. That's a significant difference.

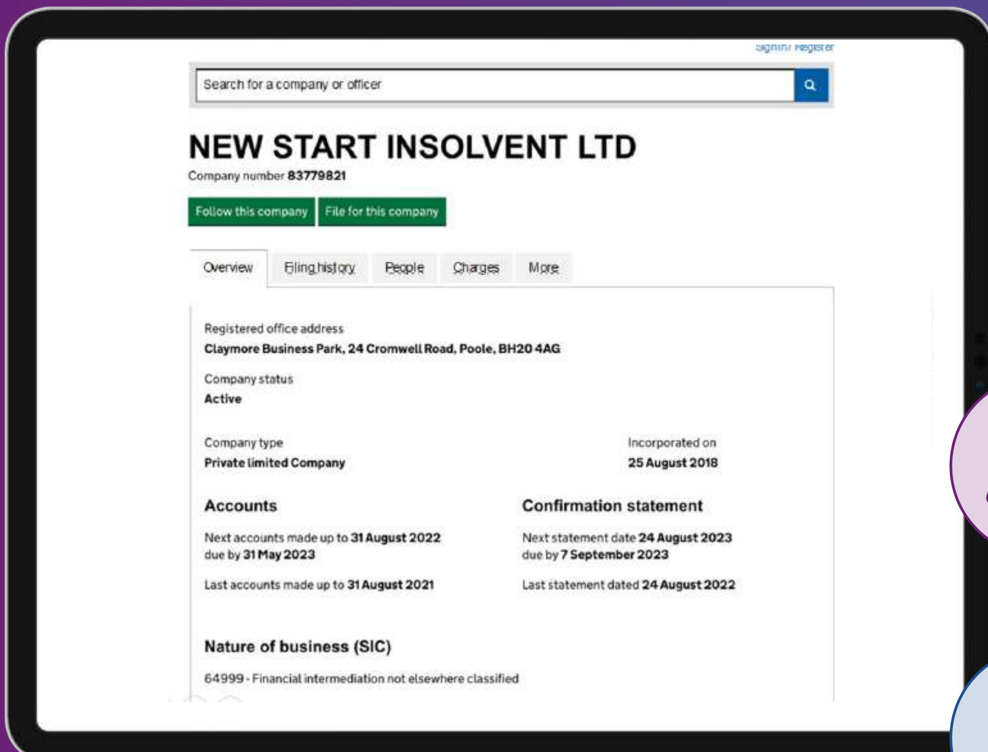
Perhaps more concerning, the credit turnover increases through 2022. In 11 months, we have witnessed almost £40m flowing through four current accounts (note that it has opened one further account). This is quite staggering when compared to its peer-expected turnover of between £1m and £2.5m for its age, size and sector.

Accounting Period	Credit Turnover	Debit Turnover	Average daily balance	# of Current Accounts
2022	39,492,715	39,745,620	1,403,707	4
Month	**Credit Turnover**			
Jan 2022	2,229,711			
Feb 2022	2,955,728			
Mar 2022	2,965,535			
Apr 2022	3,198,847			
May 2022	3,560,271			
Jun 2022	7,939,459			
Jul 2022	2,125,069			
Aug 2022	4,887,728			
Sep 2022	3,145,563			
Oct 2022	3,129,377			
Nov 2022	3,355,427			

In addition to these 8 adverse markers for this business, we've been able to link the directors to another 16 businesses, using 22 separate current accounts with over £65m of Credit Turnover flowing through them. We can't say for certain that this is a money laundering business, however armed with this valuable context, we do think this is an organisation worthy of enhanced due diligence.

EXAMPLE 3 – MAKING A SMALL FORTUNE?

In our final example, we look at a much smaller organisation; so small, in fact, that it files unaudited and abbreviated accounts. To maintain the firm's anonymity, we have called it New Start Insolvent Limited.



In this example, we can see that the business has triggered six adverse markers and two cashflow flags.

Business Profile

Age: 4

Sector: Financial intermedation not elsewhere classified

Peer Group

Age: 3-4 years

Sector: Financial service activities, except insurance and pension funding

Expected turnover: £50,000-£100,000

Adverse Markers

- No UK Director at incorporation
- No UK PSC
- No UK UBO
- Conflicting Director Nationality
- Conflicting Country of Residence
- Multiple Registered Address Changes

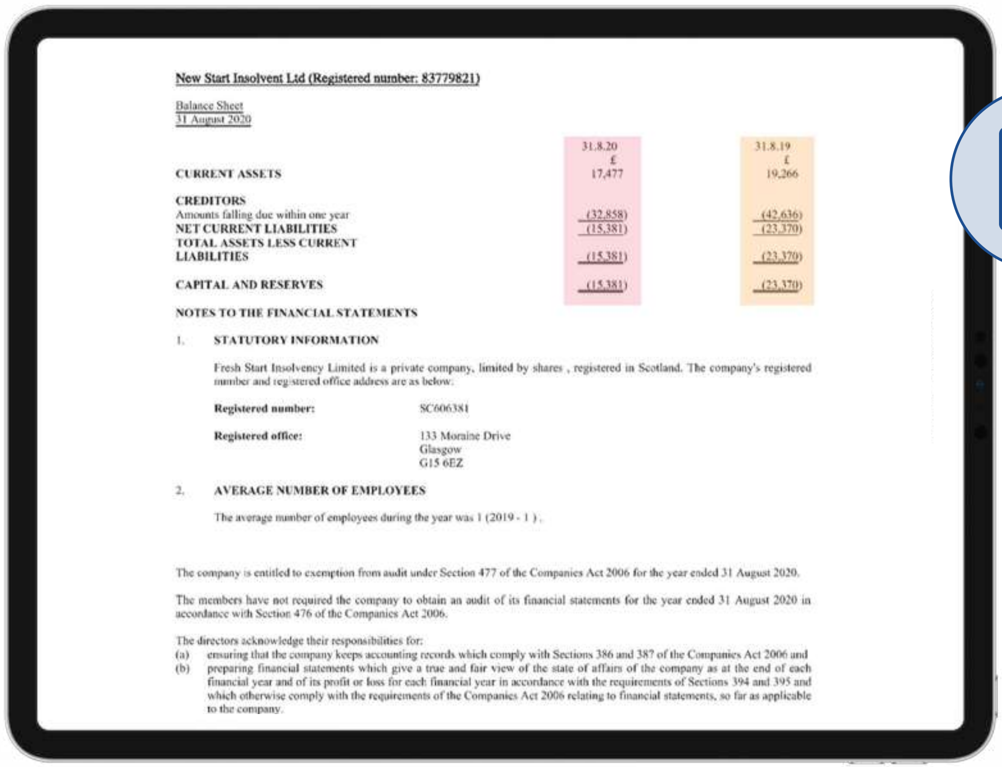
Cashflow Flags

- Credit Turnover Standard Deviation Ratio: 3
- Debit Turnover Standard Deviation Ratio: 3

We note that the director has represented his name in three different ways across a single filing. We can also see further discrepancies, including a conflicting director nationality and country of residence.

Because the company is so small, we must use total assets filed at Companies House as a proxy for turnover.

Again, as with the earlier example, we can see a significant difference in the turnover represented through our aggregate transaction data and the total asset figure filed at Companies House; a difference of almost £3m in 2020.



New Start Insolvent Ltd (Registered number: 83779821)

Balance Sheet
31 August 2020

	31.8.20 £	31.8.19 £
CURRENT ASSETS	17,477	19,266
CREDITORS		
Amounts falling due within one year	(32,858)	(42,636)
NET CURRENT LIABILITIES	(15,381)	(23,370)
TOTAL ASSETS LESS CURRENT LIABILITIES	(15,381)	(23,370)
CAPITAL AND RESERVES	(15,381)	(23,370)

NOTES TO THE FINANCIAL STATEMENTS

1. STATUTORY INFORMATION

Fresh Start Insolvency Limited is a private company, limited by shares , registered in Scotland. The company's registered number and registered office address are as below:

Registered number: SC606381

Registered office: 133 Moraine Drive
Glasgow
G15 6EZ

2. AVERAGE NUMBER OF EMPLOYEES

The average number of employees during the year was 1 (2019 - 1) .

The company is entitled to exemption from audit under Section 477 of the Companies Act 2006 for the year ended 31 August 2020.

The members have not required the company to obtain an audit of its financial statements for the year ended 31 August 2020 in accordance with Section 476 of the Companies Act 2006.

The directors acknowledge their responsibilities for:
(a) ensuring that the company keeps accounting records which comply with Sections 386 and 387 of the Companies Act 2006 and
(b) preparing financial statements which give a true and fair view of the state of affairs of the company as at the end of each financial year and of its profit or loss for each financial year in accordance with the requirements of Sections 394 and 395 and which otherwise comply with the requirements of the Companies Act 2006 relating to financial statements, so far as applicable to the company.

Cashflow Flags

- Credit Turnover Standard Deviation Ratio: 3
- Debit Turnover Standard Deviation Ratio: 3

Accounting Period	Credit Turnover	Debit Turnover	Average daily balance
Dec 2018 - Aug 2019	143,190	141,227	2,229
Sept 2019 - Aug 2020	3,239,468	3,207,721	5,777

Between September 2021 and July 2022, we then witness an extraordinary increase in credit turnover for such a small business, increasing to £11m. Also, note the average daily balance, it's very low compared to the turnover of the account.

When combining these adverse markers and aggregate industry transaction data, this small business is certainly displaying an alarming number of red flags. Again, we can't say it's definitively illegal, however such irregularities should be investigated, and the customer's risk re-assessed.

Accounting Period	Credit Turnover	Debit Turnover	Average daily balance
Dec 2018 - Aug 2019	143,190	141,227	2,229
Sept 2019 - Aug 2020	3,239,468	3,207,721	5,777
Sept 2020 - Aug 2021	7,283,935	7,31,737	10,736
Sept 2021 - July 2022	11,533,877	11,527,833	14,128

LOOKING FORWARD: A GATEWAY TO ENHANCED DETECTION AND PREVENTION

At Experian, we believe this new ability to combine adverse markers with aggregated transaction data will be truly transformational. With UK banks today hampered by a constricted view of their customers' transaction behaviour, and any attempt at creating peer group profiles restricted to internal data alone, this new service offers a gateway to collaboration and data sharing never before seen in the anti-financial crime community.

Furthermore, by combining our adverse markers with transaction alerts, you can obtain a more holistic and contextualised view of customer risk.

We will continue to work to maintain a cross-industry view of the latest characteristics and assess the third-party data needed to continually develop new adverse markers to tackle emerging risks. We are committed to ensuring the industry is armed with the latest innovations in data and analytics to continually hinder financial criminals and deliver on our mission to drive financial crime out of the UK economy.

TO FIND OUT MORE ABOUT HOW WE CAN HELP YOU DETECT AND DETER FINANCIAL CRIME, GET IN TOUCH TODAY.

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www.Experian.co.uk/powercurve

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