



6th Follow-Up Report

Mutual Evaluation of Sri Lanka

October 2021





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Cover image: The “Nine Arch Bridge” also called the Bridge in the Sky, is an iconic bridge on the Colombo – Badulla Line, Sri Lanka. Photo credit: Kasun De Silva.

SRI LANKA: 6th ENHANCED FOLLOW-UP REPORT 2021

I. INTRODUCTION

1. The mutual evaluation report (MER) of Sri Lanka was adopted in 2015.
2. This FUR analyses Sri Lanka's progress in addressing the technical compliance (TC) requirements of the recommendations being re-rated. Technical compliance re-ratings are given where sufficient progress has been demonstrated.
3. This report does not analyse any progress Sri Lanka has made to improve its effectiveness. In keeping with the APG ME Procedures, any reported developments with effectiveness are only presented in summary form and are not subject to analysis.
4. The assessment of Sri Lanka's request for technical compliance re-ratings and the preparation of this report was undertaken by the following experts:
 - *Ms. Wan Lin Chew, Ministry of Home Affairs, Singapore*
 - *Ms. Nicole van Lent, APG Secretariat*
5. Section IV of this report summarises the progress made to improve technical compliance. Section V contains the conclusion and a table illustrating Sri Lanka's current technical compliance ratings.

II. FINDINGS OF THE MUTUAL EVALUATION REPORT & FOLLOW UP

6. Sri Lanka's MER ratings¹ and updated ratings based on earlier FUR are as follows:

R.	Rating	R.	Rating
1	PC (MER 2015) ↑ LC (FUR 2018)	21	C (MER 2015)
2	PC (MER 2015) ↑ LC (FUR 2016)	22	NC (MER 2015) ↑ LC (FUR 2018)
3	LC (MER 2015)	23	PC (MER 2015) ↑ C (FUR 2018)
4	PC (MER 2015)	24	NC (MER 2015)
5	C (MER 2015)	25	NC (MER 2015) ↑ LC (FUR 2019)
6	LC (MER 2015)	26	PC (MER 2015)
7	NC (MER 2015) ↑ LC (FUR 2019)	27	C (MER 2015)
8	PC (MER 2015)	28	NC (MER 2015) ↑ PC (FUR 2019)
9	LC (MER 2015)	29	PC (MER 2015) ↑ LC (FUR 2018)
10	NC (MER 2015) ↑ LC (FUR 2016)	30	C (MER 2015)
11	LC (MER 2015)	31	LC (MER 2015)

¹ There are four possible levels of technical compliance: compliant (C), largely compliant (LC), partially compliant (PC), and non-compliant (NC).

12	NC (MER 2015) ↑ LC (FUR 2016)	32	PC (MER 2015)
13	NC (MER 2015) ↑ LC (FUR 2016)	33	PC (MER 2015) ↑ LC (FUR 2018)
14	NC (MER 2015) ↑ LC (FUR 2020)	34	PC (MER 2015) ↑ LC (FUR 2018)
15	PC (MER 2015) ↑ LC (FUR 2016) ↓ PC (FUR 2020)	35	PC (MER 2015)
16	NC (MER 2015) ↑ LC (FUR 2016)	36	LC (MER 2015)
17	NC (MER 2015) ↑ LC (FUR 2016)	37	PC (MER 2015) ↑ C (FUR 2019)
18	PC (MER 2015) ↑ LC (FUR 2016)	38	PC (MER 2015) ↑ LC (FUR 2019)
19	NC (MER 2015) ↑ LC (FUR 2016)	39	LC (MER 2015)
20	C (MER 2015)	40	PC (MER 2015)

7. Given Sri Lanka's MER, it was placed in enhanced follow-up (expedited)². Following the upgrading of nine Recommendations to LC in its 2016 FUR, Sri Lanka was moved to enhanced follow-up.

III. OVERVIEW OF PROGRESS TO IMPROVE TECHNICAL COMPLIANCE

8. In keeping with the APG Mutual Evaluation Procedures, this FUR considers progress made up until 1 June 2021. In line with the ME Procedures and FATF Methodology, the review team analysis has considered progress to address the deficiencies identified in the MER and the entirety (all criteria) of each Recommendation under review, noting that this is cursory where the legal, institutional or operational framework is unchanged since the MER or previous FUR.

9. This section summarises the progress made by Sri Lanka to improve its technical compliance by addressing the technical compliance deficiencies identified in the MER.

3.1. Progress to address technical compliance deficiencies identified in the MER

10. Sri Lanka requested re-ratings of Recommendations 32 and 40 (which were rated PC).

11. The APG welcomes the steps that Sri Lanka has taken to improve its technical compliance and as a result of this progress, Sri Lanka has been re-rated on Recommendation 32. However, insufficient progress has been made to justify a re-rating of 40.

Recommendation 32 (Originally rated PC)

12. Sri Lanka was rated PC for Recommendation 32 in its 2015 MER. Sri Lanka adopted a written declaration system for cross-border transportation of currency, however the requirement only applied to foreign currency and did not cover the full range of bearer negotiable instruments (BNIs) required by the FATF Standards. The report found that there were available powers and mechanisms in place to implement and enforce declaration requirements, but found deficiencies relating to the lack of mechanisms for Customs to share information with other competent authorities, and no mechanism for sharing declaration information with the Financial Intelligence Unit (FIU).

13. **Criterion 32.1** is *mostly met*. There is a declaration requirement for travellers who carry foreign exchange into and out of Sri Lanka, if the total value of such foreign exchange currency exceeds

² There are three categories of follow-up based on mutual evaluation reports: regular, enhanced and enhanced (expedited). For further information see the APG Mutual Evaluation Procedures.

USD 15,000 or its equivalent in other foreign currencies (Schedule I, Section 8, Part I (1), Foreign Exchange Regulations), in line with the R.32.

14. Sri Lanka has expanded the definition of foreign exchange under Section 31 of the Foreign Exchange Act, No. 12 of 2017 (FEA). Section 32 of the FEA defines 'foreign exchange' to include foreign currency and (a) deposits, credits and balances payable in foreign currency; (b) drafts, travellers' cheques, letters of credit and bills of exchange drawn in Sri Lanka and payable outside Sri Lanka in foreign currency; (c) drafts, travellers' cheques, letters of credit and bills of exchange drawn outside Sri Lanka but payable in Sri Lankan currency; (d) any document or instrument of a type customarily employed for international transfers of funds. The definition of 'currency' in the FEA, includes coins, currency notes, postal orders, money orders, cheques, drafts, travellers' cheques, letters of credit, bills of exchange, promissory notes, other electronic fund transfer cards and digital currency (Section 31, FEA).

15. The written declaration requirement above does not apply to Sri Lankan currency (LKR). However, there are strict controls for the import and export of LKR, which are only allowed in limited circumstances such as employment, education, temporary visit on holiday, business or medical treatment, or for any other similar reasons, and permission must be sought from the Head of the Department of Foreign Exchange (DFE), Central Bank of Sri Lanka (CBSL) via written application, pursuant to Part I (2) of the Order under Section 8 of the FEA (February, 2021) (the FEA Order). Customs are notified of any permissions granted by DFE. Alternatively, a person may take out of, or bring into Sri Lanka, currency not exceeding LKR 20 000 (USD 100) per person. The obligation to obtain permission from the DFE is enforceable as per section 11 (4 & 5) of the FEA 2017. Sri Lanka has demonstrated robust and effective enforcement of confiscation of undeclared currency detected at the border.

16. There is no explicit declaration requirement for the transportation of currency and BNIs via mail and cargo. The FEA Order prohibits any import and export, which may include exchange via mail and cargo of LKR above the prescribed threshold, or without the permission of the DFE.

17. **Criterion 32.2** is *mostly met*. As noted above, there is a written declaration requirement for travellers who carry foreign exchange into and out of Sri Lanka, if the total value of such foreign exchange exceeds USD 15,000 or its equivalent in other foreign currencies. It is an offence under section 119 of the Customs Ordinance if a person makes a false, or untrue declaration. However, the minor deficiency noted above in relation to LKR remains.

18. **Criterion 32.3** is *not applicable*. Sri Lanka has adopted a declaration system and not a disclosure system.

19. **Criterion 32.4** is *met*. Pursuant to Part I(1) of the FEA Order, a person is required to provide documentary evidence relating to the acquisition of the foreign exchange to the Department of Customs or subsequently to the Head of DFE of CBSL or any other person who is authorised by law to seek such information, if called upon to do so. In relation to LKR, Section 119 of Customs Ordinance provides powers to Sri Lanka Customs when dealing with any false declaration, untruly answering questions, and counterfeiting and using false documents.

20. **Criterion 32.5** is *partly met*. Since the MER, the Exchange Control Act has been repealed and replaced by the FEA 2017. The penal sanctions under Section 51(4) of the Exchange Control Act for making a false declaration were repealed.

21. Customs has powers to sanction persons who make false declarations or disclosures. Pursuant to Section 119 of the Customs Ordinance, Customs may apply a fine of 100,000 rupees (approx. USD 501) for a false declaration, and any goods, including currency in any form, related to the false

declaration are liable to forfeiture. Section 11 of the FEA 2017 provides for a fine of 1 million LKR (approx. USD 5,017) if any provision of the Act, or any order or regulations made under the FEA are contravened by anyone who is not an authorized dealer or restricted dealer, including where a person imports/exports LKR above the prescribed threshold, without DFE permission. A range of administrative penalties are available to be applied to authorized or restricted dealers who breach the obligations to obtain permission to import/export LKR, although monetary penalties are restricted to the value of undeclared currency. Section 27 of the Financial Transactions Reporting Act 2007 (FTRA) refers to a fine not exceeding 100,000 rupees (approx. USD 501) or imprisonment of either description for a term not exceeding one year, or to both such fine and imprisonment.

22. These sanctions, particularly those under the Customs Ordinance and the FEA, appear to be low and are not proportionate nor dissuasive.

23. **Criterion 32.6** is *met*. The FIU-Sri Lanka has direct access to the ASYCUDA system of Sri Lanka Customs, which contains information on all cross-border currency declarations. The FIU can also request access to the permissions granted under the FEA for cross border movement of LKR.

24. **Criterion 32.7** is *partly met*. The FIU, Customs, Sri Lanka Police, DFE, Department of Immigration and Emigration, and Department of Import and Export Control are present on the National Coordination Committee and in this regard work together to support coordinated efforts.

25. While there are no procedures or MOUs which formalise arrangements, Sri Lanka Customs has informal working arrangements with the Department of Immigration and Emigration and Criminal Investigations Department (CID) of the Sri Lanka Police when they deal with any matter relating to declaration/ non-declaration or false declaration in sharing passenger information or conducting investigations. Units of the Department of Immigration and Emigration and Sri Lanka Police are housed together with Customs at ports and airports to enable coordination. These agencies mostly work independently and share information as and when the need arises.

26. Sri Lanka advised that when funds are suspected to be linked to ML/TF, Sri Lanka Customs will contact the CID of the Sri Lanka Police to initiate investigations under Prevention of Money Laundering Act, No 5 of 2006 or Convention on the Suppression of Terrorist Financing Act No. 25 of 2005. Sri Lanka also advised that if there is a matter for investigation, the DFE would coordinate with Customs, the FIU and other competent authorities.

27. However, it is unclear to what extent agencies such as Customs and Department of Immigration and Emigration, and other competent authorities work closely together to properly coordinate efforts to detect the illegal cross-border movement of cash.

28. **Criterion 32.8** is *met*. There is no change since the 2015 MER.

29. **Criterion 32.9** is *mostly met*. Sri Lanka Customs is able to share the information, including cross border declaration information, with other customs counterparts through the Regional Intelligence Liaison Office, World Customs Organisation (WCO) or through memorandum of understanding (MOU) arrangements.

30. As noted in the MER, the FIU allows the exchange of information with foreign FIUs using an agreement or arrangement under section 16 and 17 of FTRA. Technically, cross border declaration information can be shared with the foreign FIUs under this protocol.

31. Since the MER was adopted the FIU-Sri Lanka has direct access to ASYCUDA system of Sri Lanka Customs, with access to the information on cross-border currency declarations. The ASYCUDA System retains information on declarations and disclosures that exceed the prescribed threshold, and

Sri Lanka has advised that information relating to false declarations and suspicion of ML/TF is retained separately. The MOU between the FIU and Customs requires consent from Customs before information can be shared with any third party, which may inhibit information sharing from occurring ‘rapidly’.

32. **Criterion 32.10** is *met*. The analysis in the MER relating to the application of the Code of Conduct and Customs Ordinance, and the FTRA remain valid. In relation to the new legal framework under the FEA, Section 21(1) of the FEA requires every officer or servant of the DFE of the CBSL to preserve secrecy with regard to all matters that may come to his knowledge in the performance of his duties.

33. **Criterion 32.11** is *met*. The analysis in the MER relating to the application of the ML/TF offences and the operation of provisional measures and confiscation remain valid. In relation to the new legal framework under the FEA, Sri Lanka Customs can also initiate actions in accordance with the provisions of 107, 107(A)(1) and 107(A)(2) of the Customs Ordinance, for actions including confiscation, if any person violates the FEA.

Weighting and conclusion

34. Sri Lanka has adopted a written declaration system for incoming and outgoing cross-border transportation of foreign currency and BNIs above USD 15,000. The range of BNI covered is in line with the FATF requirements. There is no separate written declaration system for transportation of Sri Lankan currency, into and out of Sri Lanka, as there are strict controls for the import and export of Sri Lankan currency (travellers, cargo or mail), which is only allowed in very limited circumstances with explicit CBSL permission, and it is enforceable if permission is not obtained. The foreign exchange declaration requirements do not explicitly extend to the transportation of currency and BNIs via mail and cargo. The available sanctions (fines) for enforcing declaration obligations appear low and disproportionate. There are available powers and mechanisms in place to implement and enforce these requirements, and there is a mechanism for sharing information with the FIU. The FIU has direct access to Customs declaration information, and Sri Lanka Customs has informal working arrangements with the Department of Immigration and Emigration and CID of the Sri Lanka Police with matters relating to declaration/ non-declaration or false declaration, and other investigations as required. **Recommendation 32 is re-rated to largely compliant.**

Recommendation 40 (Originally rated PC)

35. Sri Lanka was rated PC for Recommendation 40 in its 2015 MER. The report found that Sri Lanka’s competent authorities were generally able to provide a wide range of direct and indirect international cooperation, however there were deficiencies in the lack of mechanisms and examples of international cooperation.

36. **Criterion 40.1** is *mostly met*. As there have been no significant changes since the MER, the analysis in the MER and available material supports the criterion rating.

37. **Criterion 40.2** is *partly met*. The analysis in the MER and additional available material support the criterion rating. Since the MER, a number of additional steps have been taken to support a lawful basis, efficient and secure processes and channels for information sharing. These include:

- Sri Lanka FIU has signed an additional 15 MOUs with foreign counterpart FIUs.
- Sri Lanka Police agreed a mutual cooperation agreement with the Australian Federal Police in 2018.
- The CBSL has entered into MOUs with the Reserve Bank of India, the State Bank of Pakistan, the Bangladesh Bank and the Monetary Authority of Maldives for the purpose of strengthening the coordination among regulatory authorities. An MOU was also entered into by Sri Lanka’s

supervisors, CBSL, Securities and Exchange Commission (SEC) and Insurance Regulatory Commission of Sri Lanka (IRCSL) to enable the Bank Supervision Department (BSD) of CBSL to perform consolidated supervision, which would complement international cooperation.

38. Nonetheless, the deficiencies relating to 40.2(c) – (e) in the MER, remain. Two new proposed laws will provide additional legal basis to better support international cooperation by regulators/supervisors, however neither law is yet enacted. CBSL is in the process of drafting a new Banking Act which includes provisions for cooperation with foreign financial sector regulators. The proposed SEC law will provide an expanded statutory basis for providing international cooperation, including being able to share information with regard to regulatory functions relating to securities and investors in securities markets internationally through MOUs.

39. **Criterion 40.3** is *mostly met*. There is no change since the 2015 MER.

40. **Criterion 40.4** is *partly met*. Sri Lanka FIU, as an Egmont member, uses standard Egmont protocols in relation to feedback for FIUs. The FIU's Manual also states that where assistance is received from foreign FIU counterparts, the FIU should provide feedback on the use and usefulness of that information. INTERPOL also has a secure channel to communicate feedback. For the other authorities, there are no policy, guidelines or standards of procedure in place for providing feedback. Sri Lanka did not provide any examples nor any statistics on feedback.

41. **Criteria 40.5 – 40.7** are *met*. There is no change since the 2015 MER.

42. **Criterion 40.8** is *mostly met*. The proposed amendments to the SEC Act will provide a more comprehensive legal basis for the SEC to conduct inquiries on behalf of foreign counterparts, and exchange with their foreign counterparts all information that would be obtainable by them if such inquiries were being carried out domestically.

43. **Criterion 40.9** is *met*. The analysis in the MER and available material supports the criterion rating. Since the MER, Sri Lanka FIU has signed an additional 15 MOUs with foreign counterparts.

44. **Criterion 40.10** is *met*. The Operation Manual of the FIU provides that the FIU seek feedback on the use and usefulness of the information provided to foreign counterparts (Section 12.9). The feedback form contained in the Manual seeks information on the quality, timeliness and use of information provided. In addition, Sri Lanka is a member of Egmont and obligated to follow Egmont procedures in relation to feedback. Sri Lanka has provided feedback to all foreign FIU requests for feedback.

45. **Criterion 40.11** is *met*. There is no change since the 2015 MER.

46. **Criteria 40.12 – 40.15** are *partly met*. There is no change since the 2015 MER. As outlined above, two new proposed laws will provide additional legal bases to better support international cooperation by regulators/supervisors, however neither law is yet enacted. CBSL is in the process of drafting a new Banking Act which includes provisions for cooperation with foreign financial sector regulators. The proposed SEC law will provide an expanded statutory basis for providing international cooperation, including being able to share information with regard to regulatory functions relating to securities and investors in securities markets internationally through MOUs.

47. **Criterion 40.16** is *met*. There is a confidentiality clause in each MOU established by Sri Lanka for exchange of information between financial supervisors. Before the disclosure of information to the public or third party, the requesting financial supervisors must seek prior authorization from the

requested financial supervisors. The MOU with IOSCO also requires prior authorisation for information exchanged to be used for a purpose other than those stated in the request.

48. **Criterion 40.17** is *mostly met*. There is no change since the 2015 MER. Law enforcement authorities can also exchange available information with foreign counterparts for intelligence or investigative purposes via INTERPOL channels. Sri Lanka has provided two case examples where they shared information on money laundering, associated predicate offences, and terrorism financing with their foreign counterparts.

49. **Criterion 40.18** is *mostly met*. There is no change since the 2015 MER. The Customs Ordinance provides provisions to conduct inquiries when such matter falls within the purview of the Customs Ordinance. However, there is no specific law/provision that allow Sri Lanka Customs to use their powers to conduct inquiries or enquiries on behalf of foreign counterparts. The Sri Lanka Police is able to use its powers, including any investigative techniques, to conduct inquiries and obtain information on behalf of foreign counterparts, through INTERPOL and the FIU.

50. **Criterion 40.19** is *mostly met*. Law enforcement agencies are not prohibited from conducting joint investigations. While there is no explicit provision permitting joint investigations, there is practice that demonstrates this is possible. Sri Lanka Customs demonstrated that it is able to form joint investigative teams to conduct cooperative investigations. A case example was cited - WCO initiative - Operation Tentacle on money laundering through bulk cash smuggling/gold smuggling was conducted in 2019, where 19 countries were involved. The Sri Lanka Police is able to conduct joint investigations with the Australian Federal Police, under the provisions of the MOU signed between them, however, no case examples were shared.

51. **Criterion 40.20** is *not met*. The Sri Lankan authorities are not permitted to exchange information indirectly with non-counterparts, with the exception of the Insurance Commissioner, IRCSL, in limited circumstances. It should be noted that at the time of this report Sri Lanka was pursuing a number of statutory changes to ensure that these powers are available to relevant authorities in the future.

Weighting and conclusion

52. Whilst Sri Lanka has made some progress with signing MOUs with foreign counterparts and participating in joint international LEA investigations, the moderate deficiencies outlined in the MER remain. There is a lack of clear and documented mechanisms for the execution and prioritisation of requests. Banking information and information relating to securities and exchange have statutory provisions in their governing legislation that restricts sharing of information without a court order. Sri Lankan authorities are not permitted to share information indirectly with non-counterparts, and the ability for Sri Lanka to share supervisory information with foreign counterparts is limited. Other than the FIU, there are no policy or guidelines in place for providing feedback on information obtained from foreign authorities. Sri Lanka has indicated that they have drafted a new SEC law which will enable the SEC to share information with foreign supervisors however, the law is yet to be enacted. ***Recommendation 40 remains partially compliant.***

3.2. Brief overview of progress on other recommendations rated NC/PC

53. **Recommendation 4 (rated PC)** – Cabinet approval was received to amend the Prevention of Money Laundering Act, No. 5 of 2006 to rectify the gaps identified in the MER.

54. **Recommendation 8 (rated PC)** - A committee has been appointed to amend Sri Lanka's NPO laws and is in the process of discussing the relevant amendments including requirements under R.8.

55. **Recommendation 15 (rated PC)** - Discussions are underway to licence/register Virtual Asset Service Providers (VASPs) and steps will be taken to include VASPs as institutions engaged in finance business in the proposed amendments to the Financial Transactions Reporting Act, No. 6 of 2006.

56. **Recommendation 24 (rated NC)** – Proposed amendments to the Companies Act, No. 7 of 2007 incorporating beneficial ownership requirements for legal persons have been drafted and reviewed by the Hon. Attorney General. The AG’s comments are being reviewed by stakeholders including the Registrar of Companies and the FIU.

57. **Recommendation 26 (rated PC)** – The FIU continues to conduct risk-based AML/CFT supervision, and all relevant regulators were advised to extend the fit and proper criteria for shareholders and beneficial owners. The Department of Foreign Exchange issued directives requiring money changers to include fit and proper criteria for senior management, shareholders and beneficial owners.

58. **Recommendation 28 (rated PC)** – The FIU continues to undertake AML/CFT supervision of the DNFBPs sector.

59. **Recommendation 35 (rated PC)** – Proposed amendments to the Financial Transactions Reporting Act, No. 6 of 2006 (FTRA) include a revision of the penalty structure. Cabinet approval has been received to amend the FTRA.

IV. CONCLUSION

60. Overall, Sri Lanka has made some progress in addressing the technical compliance deficiencies identified in its MER and has been re-rated on Recommendation 32.

61. In light of the progress made by Sri Lanka since its MER was adopted, its technical compliance with the FATF Recommendations is as follows as of the reporting date 1 June 2021:

R.	Rating	R.	Rating
1	PC (MER 2015) ↑ LC (FUR 2018)	21	C (MER 2015)
2	PC (MER 2015) ↑ LC (FUR 2016)	22	NC (MER 2015) ↑ LC (FUR 2018)
3	LC (MER 2015)	23	PC (MER 2015) ↑ C (FUR 2018)
4	PC (MER 2015)	24	NC (MER 2015)
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12	NC (MER 2015) ↑ LC (FUR 2016)	32	PC (MER 2015) ↑ LC (FUR 2021)
13	NC (MER 2015) ↑ LC (FUR 2016)	33	PC (MER 2015) ↑ LC (FUR 2018)
14	NC (MER 2015) ↑ LC (FUR 2020)	34	PC (MER 2015) ↑ LC (FUR 2018)
15	PC (MER 2015) ↑ LC (FUR 2016) ↓ PC (FUR 2020)	35	PC (MER 2015)

16	NC (MER 2015) ↑ LC (FUR 2016)	36	LC (MER 2015)
17	NC (MER 2015) ↑ LC (FUR 2016)	37	PC (MER 2015) ↑ C (FUR 2019)
18	PC (MER 2015) ↑ LC (FUR 2016)	38	PC (MER 2015) ↑ LC (FUR 2019)
19	NC (MER 2015) ↑ LC (FUR 2016)	39	LC (MER 2015)
20	C (MER 2015)	40	PC (MER 2015)

62. Sri Lanka has 32 Recommendations rated C/LC. Sri Lanka will remain in enhanced follow-up, and will continue to report back to the APG on progress to strengthen its implementation of AML/CFT measures. Sri Lanka's 7th progress report is due 1 June 2022.