THE FOUNDATION FOR
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# Policy and Regulatory Framework for Remittance - Sri Lanka

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## EXECUTIVE SUMMARY


Sri Lanka has a large migrant worker population, estimated to be around 1,500,000 of which 500,000 are considered to be illegal migrants. The formal worker remittances to Sri Lanka amounted to US$1,918 million in 2005, and accounted for 8% of GDP. The main sources of remittances were Middle East (56.5%), European Union (18.5%), North America (6.5%), other European countries (6.5%), and Far Eastern countries (4.5%).

The migrant workers have helped Sri Lanka to reduce its unemployment levels and to increase labour force participation rates. Total unemployment which was around 18% in 1981 has fallen to 7.7% by 2005. Furthermore, poverty rates in districts which have sent the largest numbers of workers abroad have experienced larger improvements in income levels. It has been suggested that about 15% of the total population and about 25% of low-income households have benefited from remittances.

There are 25 financial agencies authorised by the Central Bank of Sri Lanka to engage in foreign exchange transactions. These include 22 Licenced Commercial Banks (LCBs), two other financial institutions and the post office. There are several formal schemes which give incentives on remittances transfer through formal channels. These include foreign currency denominated Sri Lanka Nation Building Bonds and exemptions on custom duties on goods brought into the country. Further, there are a number of other incentives related to migration and remittances such as the services offered by the Sri Lanka Bureau of Foreign Employment.

In spite of the formal incentives offered, remittances sent through informal channels are estimated to be around 50%, a proportion which seem to have grown rapidly in recent years. The main sources of informal remittances are: undocumented workers; workers with expired visa; and first-time migrant workers. It has been estimated that around 700,000 to 1,000,000 people have left the war-stricken north and east of the county without official travel documents.

This study concludes that the regulatory framework for remittances in Sri Lanka is restrictive. In response, the study suggests a number of mechanisms to make the remittance market more efficient. This includes separating the remittances market from the rest of the foreign exchange market and relaxing the documentary requirements for smaller remittances. It is envisaged that through these methods, the volume of funds channelled through informal remittances could decline while enhancing the formal remittances. Further, the study also highlights that the competition in the remittances market is limited. The access to remittances services by Sri Lankan workers abroad and their relatives in the country are also constrained by the restrictive licensing policy and excessive regulations. It is suggested that reforms in the remittances market should aim at increasing competition among remittances service providers and expanding the access to such services in Sri Lanka and abroad.

## 1. Introduction

In 2005, the formal worker remittances to Sri Lanka amounted to US$1,918 million. The main sources of remittances were Middle East (56.5%), European Union (18.5%), North America (6.5%), other European countries (6.5%), and Far Eastern countries (4.5%). Table A1.1 indicates official worker remittance figures. This table does not include the informal remittances which are considered to be as much as 50% of official remittances (Ratha, 2005).

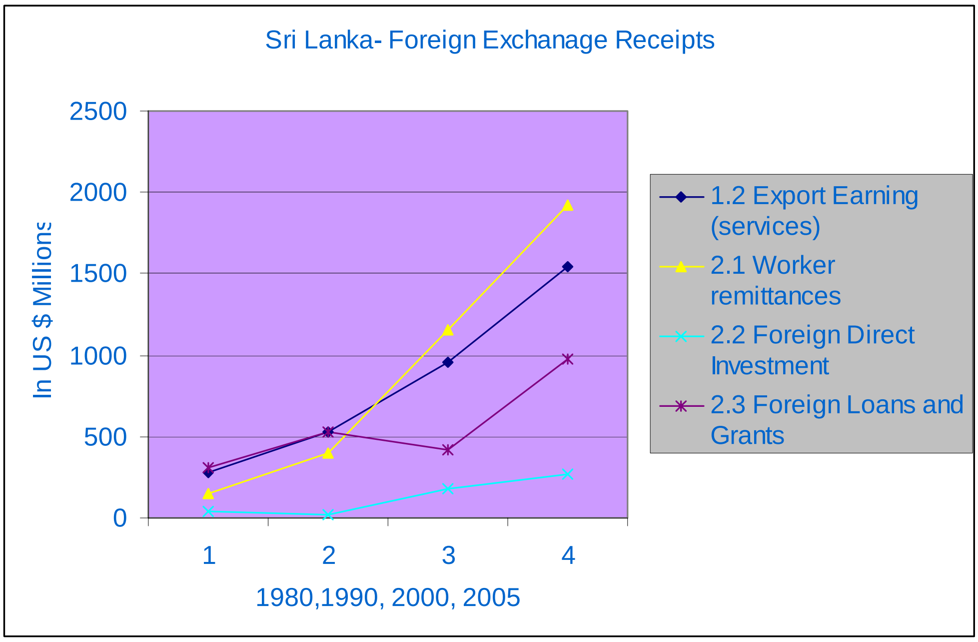
The stock of Sri Lankan workers abroad is around one million according to official sources, but at least another half a million workers are estimated to be abroad. The official worker remittances accounted for 8% of the country's GDP in 2005. During the last two decades, worker remittances have grown steadily surpassing major foreign exchange earners such as tea, tourism, garments and textiles. Worker remittances have steadily which has helped the country to finance a growing import bill and to reduce the burden of servicing foreign debts. This is significant in the context of the growth rate of around 5% in GDP and the unsteady and slow growth in foreign direct investment and foreign aid as shown in diagram 1.

Table 1: Sri Lanka- Major Sources of Foreign Receipts in US$ Mn for 1980 to 2005

| Sources of Foreign Receipt | 1980 | 1990 | 2000 | 2005 |
|---|---|---|---|---|
| 1.1 Export Earnings (goods) | 1064.7 | 1983.9 | 5522.3 | 6348.7 |
| 1.2 Export Earning (services) | 279.1 | 531.0 | 953.0 | 1540.2 |
| 1.3 Total earnings | 1343.8 | 2514.9 | 6475.3 | 7888.9 |
| 2.1 Worker remittances | 152.3 | 400.7 | 1160.0 | 1918.5 |
| 2.2 Foreign Direct Investment | 42.9 | 24.4 | 175.1 | 272.2 |
| 2.3 Foreign Loans and Grants | 307.0 | 526.3 | 422.0 | 972.0 |
| 3.0 Significance (%) of Worker Remittances in | | | | |
| 3.1 Trade Balance | 15.4 | 57.0 | 64.5 | 76.2 |
| 3.2 Total imports | 7.4 | 14.9 | 15.8 | 21.6 |
| 3.3 Total Foreign Earnings | 11.3 | 15.9 | 17.9 | 24.3 |
| 3.4 Foreign Loans and Grants | 49.6 | 76.1 | 274.9 | 197.3 |
| 3.5 Debt Service ratio as a % of receipts from merchandize exports, services and private remittances | 16.0 | 15.0 | 12.2 | 6.3 |
| 3.6 GDP | 3.8 | 5.0 | 7.0 | 8.1 |

*Source: CBSL, Annual Reports*

Diagram 1: Sri Lanka -Trends in Foreign Exchange Receipts




*Source: Selected Data in Table 1*

## 2. Effect on Labour Markets

The migrant workers have helped Sri Lanka to reduce its unemployment levels and to increase the labour force participation rates. Total unemployment which was around 18% in 1981 had fallen to 7.7% by 2005. The female unemployment which was 31% in 1980 has fallen to 11.9% in 2005. The male unemployment rate which was 13.3% in 1980 has fallen to 7.7% by 2005. The poverty rates in districts which have sent the largest numbers of workers abroad have experienced larger improvements in income levels (Sriskandarajah, 2002).

Approximately 80% of migrant workers have been married females in the age group of 30-45 years and many have not worked previously as wage earners. The average educational attainment of a female worker is around nine years of schooling. The female workers come from all districts, but mainly from Colombo, Gampaha and Kalutara districts which are in the Western region. The funds received by families of migrant workers have been used mainly for personal consumption, education of children and re-construction of houses (abid).

## 3. Licensed Remittance Arrangements

Migrant workers remitting their savings to families in most regions of Sri Lanka has not been problematic. However, remitting of funds to families in North and East Regions through formal channels has been almost impossible due to the prevailing ethnic conflict. The commercial banks which are the approved foreign exchange agents of the Exchange Control Department could provide only a limited range of banking services in a few townships within the two regions. It is mainly the microfinance institutions (MFIs) that have provided financial services in these two regions, but the MFIs were not licensed to accept deposits or provide remittance services.

The financial system in Sri Lanka and the associated fund transfer system is highly fragmented. There are two types of banks, i.e., Licenced Commercial Banks (LCBs) and Special Licensed Banks (SLBs). The former category is allowed universal banking have foreign currency banking units (FCBUs) and also provide remitting services. The latter category can provide only some limited banking services and that do not include remitting services. The Central Bank licenced non-bank financial institutions (NBFIs) are mainly finance companies and leasing companies, which are not authorised to engage in remittance services. In addition to the 22 LCBs, only three other financial institutions are authorised to provide remittance services.

Remittance services are a part of the overall foreign exchange market in the country. Remittance services are provided in an oligopolistic market setting, while the exclusiveness, over regulation and inadequate access to formal remittance channels both in Sri Lanka as well as in the labour importing countries have contributed to the rapid growth of informal remittances.

International fund transfer companies such as Western Union and Money Gram have been active in Sri Lanka in addition to formal correspondent banking arrangements. Local LCBs too have adopted electronic fund transfer methods (Abewickrama, 2005). The workers who have migrated informally i.e., without official passports and employment visas, come largely from North and Eastern regions of the country. These workers had to use informal fund transfer mechanisms to remit their money to relatives in Sri Lanka; and such funds have been considerable.

## 4. The Remittance Market in Sri Lanka

The worker remittances which are the net savings of Sri Lanka workers abroad are received through several different channels. These include:

(i) remittances received through banks which are approved foreign exchange dealers;
(ii) funds brought personally when travelling into the country; and
(iii) remittances that are received through informal channels.

### 4.1 Worker Remittances through Formal Channels

There are 25 financial agencies authorised by the Exchange Control Department (ECD) of Central Bank of Sri Lanka to engage in foreign exchange transactions. In line with the Banking Act, all 22 licensed commercial banks are appointed foreign exchange transaction agents. In addition, three other institutions, the state owned National Savings Bank, Bank of Ceylon and MBSL subsidiary and the Sri Lanka Post Office are authorised to engage in restricted foreign exchange transactions.

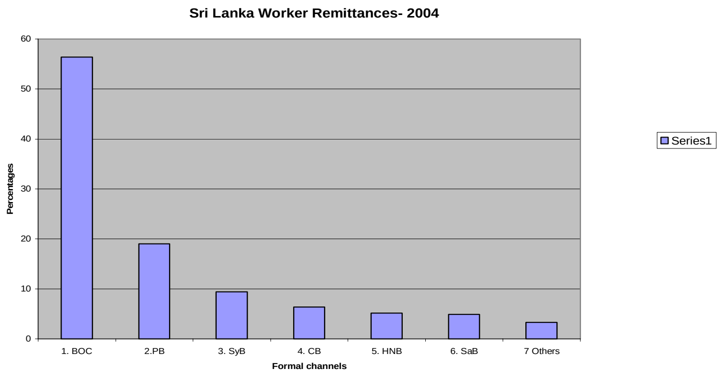
Table 2: Sri Lanka- Authorised Foreign Exchange Transaction Agents

| Name of Agent | Worker-Remittances Received in 2004 in US$ Mns | % Of total remittances | Remark |
|---|---|---|---|
| 1.Bank of Ceylon (BOC) | 881.4 | 56.4 | State owned (295 branches) |
| 2.Peoples Bank (PB) | 232.0 | 19.0 | State owned (320 branches) |
| 3. Seylan Bank (SyB) | 147.5 | 9.4 | Private owned local bank (109 branches) |
| 4.Commercial Bank (CB) | 93.4 | 6.0 | Private owned local bank (114 branches) |
| 5. Hatton National Bank (HNB) | 81.6 | 5.2 | Private owned local bank (142 branches) |
| 6. Sampath Bank (SaB) | 76.1 | 4.9 | Private owned local bank (63 branches) |
| Others* | 51.2 | 3.3 | |
| Total | 1563.9 | 100.0 | |

*Source: CBSL and WB Report, 2006*

*Note: * Others are remaining 5 domestics LCBs, 11 foreign LCBs, National Savings Bank, and a Bank of Ceylon and MBSL subsidiary MMBL Money Transfer Ltd.*

Diagram 2: Sri Lanka Worker Remittances in 2004 Classified by Authorised Agents




*Source: Table 2 above.*

### 4.2 Worker Remittances through Informal Remittances

Remittances sent through informal channels are estimated to be around 50%, a proportion which seem to have grown rapidly in recent years. There are three main types of informal remittance channels:

(i) undocumented workers;
(ii) workers with expired visa; and
(iii) first-time migrant workers.

The number of workers who migrate from Sri Lanka without valid papers has increased. The workers from conflict affected northern and eastern regions are among the vast majority of these unofficial workers. The total number of workers who have left north and east regions of Sri Lanka without official travel documents are estimated to be in the range of 700,000 to 1,000,000 (see end note 9.5). The parents and other relatives of these undocumented workers continue to receive funds mainly through informal remittance channels.

In addition to these undocumented workers, there are some whose visas have lapsed and are waiting for renewals or fresh visas from another country. These workers who are unable to produce documents which the Exchange Control Department has specified as necessary for remitting funds to Sri Lanka also use informal channels to transfer their savings (see end note 9.4).

A third category who uses informal remittance channels is the first time migrant workers. These workers have gone to work in foreign countries with all the required documents, but face difficulties in sending funds to Sri Lanka until they establish contacts or open accounts with a corresponding bank of a Sri Lankan authorised agent in that country. The banks often require customers to deposit a minimum amount of funds as a condition of opening new accounts. The period which a migrant worker is required to collect such funds can be as much as four to six months. On the other hand, the first time workers would have borrowed money in Sri Lanka to meet the cost of employment agents, and would have to make repayments almost immediately. This also makes it necessary for migrant workers to send some funds back to Sri Lanka through informal channels (see end note 11). It is reported that in Italy about 45% of migrant workers use informal channels to send their remittances as they are not familiar with the procedures and the language used in Italian banks (Giggi, 2006). According to Ratha (2006), the funds remitted to Sri Lanka annually through informal channels, could be as much as half of formal remittances received in the country (Lanka Business Online, Dec 2005)

## 5. Rules Relating to Mobilisation of Deposits by Non-bank Financial Institutions

### 5.1 LCB and Other Authorised Foreign Exchange Dealers.

As noted earlier, under the Banking Act and the Exchange Control Act, CBSL has permitted licensed commercial banks, and three other financial agencies to mobilise remittances in foreign countries. These authorised agents in foreign exchange transactions have their collecting agents or correspondent agents in foreign countries. The foreign agents when accepting funds to be remitted to Sri Lanka have to collect personal identification, visa particulars and the source of funds as per ECD reporting requirements. At the time of en-cashing or depositing the funds in Sri Lanka, similar particulars have to be recorded from recipients. The authorised agents have to forward particulars of senders and recipients on amounts less than US$5000/weekly; and on the following day/immediately electronically, in respect of funds exceeding US$5000 (see end note 5).

### 5.2 Financial Institutions Excluded from the Remittance Market

Since the financial system in Sri Lanka is fragmented, the facility to immediately transfer funds to other financial institutions as deposits is normally not available; and if such transfer is desired it has to be done through separate intervention by the clients. Direct domestic deposit mobilisation is permitted only to licensed specialised banks, licensed finance companies and leasing companies. The credit cooperatives (TCCSs and CRBs) and Samurdhi Banking Societies are registered by the Cooperative Development Commissioner and Samurdhi Authority respectively, they accept deposits from members as well as from non-members. However, these authorities are of the view that the Banking Act and the Finance Companies Act are not applicable to them. The largest part of the MFI sector in Sri Lanka is made up of TCCSs, CRBs and SBSs. The private sector MFIs (MF-NGOs and MF-INGOs) are not licensed to accept deposits, however many do accept deposits since the law is not strictly enforced. Nonetheless, a major constraint on microfinance activities is the ambiguity that prevails with regard to the powers of private sector MFIs to accept deposits and it has created a very uneven playing field (see Annex Table 5).

Private non-bank institutions, particularly credit unions in many labour importing countries provide greater access to migrant labour by accepting funds within a less formal setting (Gaggi, 2006). The remittance regulators in Sri Lanka have not yet considered this aspect of providing greater access to money transfer services to workers abroad. However, such expansion of access to remittance services is likely to further promote formal transfer of funds.

## 6. Interest Rates and Prudential Regulations Affecting Non-Bank Sector Growth and Competitiveness

Interest rates in Sri Lanka are largely influenced by the policy makers. The CBSL basic repo rates provide the signals for interest rate movements in the banking sector. As stated in the IMF country paper on Sri Lanka, the CBSL relies mostly on the interest rate and credit channels for the transmission of monetary policy to prices and output. Thus, a drop in policy rates is expected to lead to a decline in market-determined interest rates and to an increase in lending. This would in turn have a positive effect on economic activity while putting upward pressure on inflation (IMF, 2004) (see end note 10).

In 2005, CBSL issued new regulation on interest rates for non-bank financial institutions. CBSL directs that annual interest on less than one year time deposits should not exceed three percentage points above the Treasury Bill (TB) rates and interest rates on longer time deposits should not exceed six percentage points (see end note 7). There are no prudential regulations relating to deposits linked to remittances as non-bank financial institutions are not authorised to provide remittance services.

## 7. Tax Treatment of Remittances

There are several schemes which give tax exemptions on remittances. Following the 2006 Budget proposals, the Ministry of Finance launched the foreign currency denominated Sri Lanka Nation Building Bonds (SLNBB) through the Public Debt Department of the CBSL under the Foreign Loans Act No. 29 of 1957.

State-owned Bank of Ceylon (BOC) managed the issue of SLNBBs, with Deutsche Bank AG acting as custodians. To launch the process, the government started with a smaller US$25million tranche and raised the balance, depending on the fiscal requirements and buyer response. The minimum subscription for the five-year issue starts at US$500, Sterling Pounds 250 or Euro 500. The patriotic bond carries a six-month floating rate of interest pegged to US treasuries or equivalent in British or German government securities. As at June 2006, the dollar denominated bonds would carry a rate of 5.1356 percent, sterling denominated ones 4.8133 percent and Euro at 3.8259 percent, based on current rates. However, in 2005 the Sri Lankan government paid LIBOR plus 95 basis points on a US$100million syndicated loan structured by Citibank. In 2006, the government was expected to pay to LIBOR plus 150 basis points or (4.7+1.5 percent) on the bonds marketed by Citibank.

The SLNBB investors are entitled to import a vehicle of their choice with a payment of 25% of CIF value in lieu of Custom Dues, VAT & import duty. The CIF value of the vehicle cannot exceed 20% of the face value of the bond acquired by the investor, subject to a maximum value of US$35,000.

The closing date of the initial US$25million SLNBBs was extended a year, i.e., Feb 2007 in August 2006 as the subscriptions were slow to come in.

## 8. Other Incentives Relating to Migration and Remittances

The government policy on labour migration has been pro-active, and has considered labour migration as a way of solving unemployment in the country. The government policy interventions in a number of areas such as insisting on formal labour contracts and health insurance have been helpful to mitigate migrant workers' risks. The Sri Lankan government policy on worker migration has been more in line with the General Agreement on Trade in Services (GATS), Mode 4 proposals on movement of natural persons (ACCI, 2002).

### 8.1. Sri Lanka Bureau of Foreign Employment

Foreign employment by Sri Lankan workers is regulated under the Foreign Employment Act of 1995. The Sri Lanka Bureau of Foreign Employment (SLBFE), established under the Act performs the following functions:

- Registration and licensing of foreign employment recruiting agencies in the country.
- Formulate and implement policies in relation to Sri Lankan workers going for foreign employment.
- The policy interventions taken by SLBFE are indicated in Table 3.

Table 3: The main areas of policy intervention by SLBFE

| Item | Policy Intervention | Responsibility |
|---|---|---|
| 1. | Traveling Cost | FE |
| 2. | Accommodation | FE |
| 3. | Medical care/insurance | FE |
| 4. | Cost of recruitment | FE* |
| 5. | Sri Lanka Registration and insurance | SLBFE* |
| 6. | Training prior to departure for employment | SLBFE* |
| 7. | Minimum wages | SLBFE* |
| 8. | Minimum contract details including period of service | SLBFE and FE* |

*Notes: 1. FE= Foreign Employer.*
*2. *In these fields extent of non -compliance of regulations is considerable*

(i) Over 260 employment agents are registered by a SLBFE. Many employment agents in Sri Lanka charge a sum approximating about 3 months salary as recruitment fee. This has made it essential for most of the first time family workers to borrow money, often from money lenders and relatives (see note 11 for an estimate of these costs).

(ii) The workers who go on foreign employments for the second and subsequent times make employment agreements with the employers on their own and often do not seek SLBFE registration and insurance.

(iii) A minimum wage of US$150 for household workers was announced by SLBFE in June 2005. This is complied with only in a few countries. The main household worker employing country, Saudi Arabia did not agree to this minimum wage requirement.

(iv) The main benefits provided to Sri Lankan workers by foreign employers are: (a) free sharing accommodation, (b) basic medical care, and (c) air transport at the beginning and end of two year employment contract. The quoted salary includes the food allowance. The main benefits provided by SLBFE are (a) training to first time household workers, (b) evacuation of Sri Lankan workers in the event of a crisis such as war, (c) negotiating benefits such as health care, two year contract period, and minimum wages where other party agrees.

### 8.2. Incentives for Formal Remittances

(i) As noted earlier, worker remittances are tax exempted in Sri Lanka. An individual returning to the country can bring upto US$10,000 without prior permission, while a Sri Lankan travelling abroad can buy upto US$5000 without appropriate exchange control permission.

(ii) Workers are exempted from custom duties on goods they purchased on return to Sri Lanka, up-to SLRs50,000/. This facility is extensively used by Sri Lankan foreign workers on their return to purchase household utility items such as television and refrigerators. The value of items items they purchase are considered to be about 10% of an average worker savings.

(iii) There is a Non-Resident Foreign Currency (NRFC) Account facility available to Sri Lankan foreign workers. This is a major attraction to workers who save, in view of the depreciating Sri Lankan currency and the growing inflation and low interest rates. This facility is being widely utilised by high wage earning Sri Lankan workers. As at end June 2006, the total NRFC funds with LCBs amounted to US$2065 mn (see end note 12).

(iv) LCBs are permitted to offer Rupee drafts facility for remittances in addition to other remittance methods. LCBs have arrangements with their correspondent banks in Middle East countries to issue Sri Lanka Rupee drafts to migrant workers by accepting local currency. With this method receiving client pays only a nominal sum of SLR 50/ per transaction. This fund transfer devise is very popular among household workers in Middle East countries.

(v) LCBs are permitted to give foreign currency housing loans to Sri Lankan foreign workers. This is very rarely being used by low wage earning Sri Lankan workers (see end note 4).

## 9. Conclusion

The remitting services in Sri Lanka are an exclusive function of 22 licensed commercial banks and National Savings Bank, MMBL and the Sri Lanka Post Office. Although there is a large network of other financial institutions, they are not licensed to engage in providing remittance services.

Ratha and Reidberg (2005) have suggested that developing country foreign exchange markets for worker remittances could be restructured to be a separate market. In Sri Lanka, there is a need to recognise remittance services as a self-standing industry separate from banking services. An inclusive financial system between banks and other financial service providers should be promoted. This would create greater competition and increase access to formal remittance service providers both within Sri Lanka and also in foreign countries.

The oligopolistic market in the remittance services in Sri Lanka has been created through strict licensing rules and the demanding documentation requirements from clients. It appears the regulations enforced by Sri Lankan authorities are in excess of what is considered proportionate legal and regulatory requirements (Cirasino and Hollanders, 2006) (see note 2). For small remittances up-to US$200, only limited identification should be required. In some countries, documented personal identification is not required to send a small sum of money (Gaggi, 2006). Relaxing of documented evidence requirements on small remittances can have the impact of expanding the use of formal remittance services while discouraging the use of informal channels.

The polices followed by the Government through SLFEB, seem to promote worker productivity and foreign employment while providing some relief to the employed abroad, particularly in Middle East countries in certain circumstances (see end notes 8 and 9 ).

About 15% of the total population and about 25% of low income households have benefitted from remittances. About half of all migrant workers come from poor regions in the country. The income-augmenting role of remittances has been particularly important in the North and East regions and the funds have come mainly through informal channels. The government programmes also stress the poverty alleviation role played by income transfers of migrant workers. The families of Sri Lankan workers who receive remittances use them mainly to meet consumption and educational expenses.

The recent policies on financial sector have been moving in the direction of financial repression. The interest rates are suppressed, even beyond the inflation rate. As noted, the 2005 direction of NBFI Department on interest rates payable on deposits and the relaxed monetary policy reflect the policy direction (see end notes 7 and 10.1 through 10.3 ).

## End Notes

### Note 1: Definition of Remittances

Three streams of monetary transfers flowing into countries are included in remittances and published annually by the IMF in its BOP Statistics Yearbook and categorised as: Workers remittances; Compensation of employees; and Migrant transfers. However, the term "remittances" has come to include more than the above in the eyes of a number States, institutions and experts. In this study, migrant remittance is defined broadly as the monetary transfers that a migrant makes to the country of origin. This can include:

- Personal transfers of funds from a migrant worker or permanent migrant to a recipient, usually in the country of origin.
- Funds invested, deposited or donated by the migrant to the country of origin. In other words, financial flows associated with migration.

*(Source: MIGRANTS' REMITTANCES [Background note], 2004, United Nations Office of the High Representative for the Least Developed Countries, Landlocked Developing Countries and Small Island Developing States [UN-OHRLLS] and IMO)*

### Note 2: General Principals of Remittance Market

Cirasino and Hollanders of World Bank (2006) have stated five general principles on market for remittances; namely, GP1 The market for remittances should be transparent and have adequate consumer protection; GP2 Improvements to payment system infrastructure that have the potential to increase the efficiency of remittance services should be encouraged; GP3 Remittance services should be supported by a sound, predictable, non-discriminatory and proportionate legal and regulatory framework; GP4 Competitive market conditions, including appropriate access to domestic payments infrastructures, should be fostered in the remittance service industry, and GP5 Remittance services should be supported by appropriate governance and risk management practices

### Note 3: Formal and informal worker saving remittances:

The Hundi money transfer system has been very popular in India, Pakistan, Bangladesh and Sri Lanka.
In 2005, Sri Lanka is estimated have got around US$ 2.5 billion worth of remittances which are roughly ten percent of your GDP, according to Dilip Ratha, Senior Economist and one of the authors of the World Bank study on worker remittances. Ratha says around US$ 1.7 billion is remitted to Sri Lanka annually through legal channels, but another 50 percent of this, flows is through informal channels.

*(Source: Lanka Business Online, Dec 2005)*

### Note 4: Housing Loans in Foreign Currency to Sri Lankans Working Abroad.

Exchange Control Dept. Operating Instructions dated 04-09-2002. Reference No: 06/02/12/2002
Banks are permitted to grant loans in foreign currency to Sri Lankans working abroad to purchase or construct houses in Sri Lanka. Repayments of loans too shall be in foreign currency.

*(Source: CBSL, AR, 2002)*

### Note 5: Monitoring of Foreign Exchange Dealings over US$ 5000

The Financial Transactions Reporting law mandates banks, finance companies, leasing companies, casinos, accountants, auditors and lawyers to report any transactions that appear to be 5,000 dollars and above to the authorities. Sri Lanka has also enacted an anti money laundering law, which makes it illegal for people to 'wash their dirty money' or 'legitimise their ill-gotten gains,' by disguising the sources, changing the form, or moving the funds to a place where they are less likely to attract attention. The illegal activities cover terrorism, organised crime, illicit arms sales, drug trafficking, human trafficking, prostitution, insider trading, bribery, computer frauds and so forth.

*(Source: Lanka Business on Line, Feb 2005)*

### Note 6: CBSL Guidelines on Customer Due Diligence

'Know Your Customer' Procedures briefly is:

(i) Have sufficient information on the identity of the customer.
(ii) Be satisfied that the prospective customer is who he/she claims to be.
(iii) Ensure that the information obtained in respect of the customer in the normal course of business is used effectively for the prevention of money laundering/terrorism funding.

*(Source: Directions, Determinations, Notices and Guidelines issued to Licensed Commercial Banks by CBSL, Annual Report, 2002)*

### Note 7: Cap on Interest Rates

Finance Companies (Interest) Direction No 2 of 2005, issued on 31.01. 2005 for Non-Bank Financial Institutions is as follows:

Section 2 (a) maximum annual rate payable on time deposit:

(i) The weighted average yield applicable to 364 day Treasury Bill issued during the immediately preceding quarter by 3 percentage points if such deposit carry a maturity period of 12 months or less;
(ii) The weighted average yield applicable to 364 day Treasury Bill issued during the immediately preceding quarter by 6 percentage points if such deposit carry a maturity period of more than12 months.

*(Source: CBSL, Annual Report, 2005)*

### Note 8: Sri Lanka Govt. Intervention to Promote Foreign Employment.

The Sri Lanka Bureau of Foreign Employment (SLBFE) is a Public Corporation established by Act of Parliament in 1985.The key Departments of the SLBFE on worker migration are as follows.

- Regulation of activities of Employment Agencies.
- Settlement of disputes between employers, employees and Recruitment Agents.
- Awareness programmes.

- Welfare of migrants and their families.
- Reintegration programmes.
- Identifies new foreign employment opportunities and development programmes.
- Training and certification of prospective migrants.
- Maintenance of a Data Bank.
- Monitors progress through Labour Attaches and Welfare Officers.
- Co-ordinates with Missions
- Undertakes market research

Note 9: Other interventions by the Sri Lanka Government during 2003- 2006

9.1.1 Evacuation of migrant workers-2003

The government has made contingency plans for migrant workers in the Middle East in the event of war over the Iraqi weapons issue. Plans have been drawn up for the safety and welfare of more than 500,000 Sri Lankan workers in Saudi Arabia and Kuwait, including evacuation to safer places should war break out. (*Source: Daily News, Jan 2003)*

9.1.2 Evacuation of Sri Lanka Workers in Lebanon- 2006

Some 80,000 workers have sought help of Sri Lankan embassy in Beirut. Over 8000 have been brought back to Sri Lanka by August 2006. Source (Sunday Times, August 2006).

9.2 Compensation to families of dead migrant workers-2003

The government paid a total of Rs1.4 million as compensation to the dependents of 145 Sri Lankan migrant workers who died overseas last year. In addition, 55 workers who have died had their funerals in their respective countries of assignment, with the legal consent of family members. Out of the 200 victims, 105 were males; 95 were females. Most of the workers died in Saudi Arabia, UAE, Lebanon, Kuwait, Jordan, Yemen, Qatar and Oman. A few deaths were reported in Bangladesh, Maldives, Cyprus and Italy. One hundred and fifteen deaths occurred due to natural causes, while others died from accidents, suicides and homicides.

9.3. Compensation for Gulf workers

The final batch of 1,750 Sri Lankan migrant workers who lost their jobs due to the Gulf War in Kuwait in 1990 will be paid compensation next month under a special grant of Rs650 million made by the UN Compensation Committee. Each worker is expected to receive Rs350,000. Nearly 98,000 Sri Lankan workers in Kuwait lost their jobs when Iraqi forces invaded Kuwait. About 90 percent of them were employed as domestic workers in Kuwait; some were employed in large-scale industrial parks and garment factories. Most of them were evacuated and airlifted to Sri Lanka on special charter flights provided by the government.

9.4 Grace period for Sri Lankan workers in Syria-2003

About 2,050 irregular Sri Lankan migrants have been allowed to remain in Syria for three months following the Minister of Employment and Labour talks. Except for 240 Sri Lankans, the rest were undocumented. The number of irregular migrants to Syria has increased due to tensions in the neighbouring states and the economic advantage of staying in Syria. (*Source: Sunday Observer, Jan 26, 2003)*

## 9.5 Return of refugees, IDPs-2003

In 2003 the government and the LTTE have agreed to take measures to facilitate the return of more than one million Sri Lankan refugees scattered across the world, with priority accorded to some 64,000 Tamils in 111 refugee camps in Tamil Nadu, India. The decision was reached at a UNHCR-sponsored workshop attended by senior representatives of the Sub-Committee on Immediate Humanitarian and Rehabilitation Needs. Both parties noted that persons displaced by war have the right to return to their country of origin as stated in the International Human Rights Charter and the Covenant of Civil and Political Rights.

About 700,000 Tamils fled the country after an ethnic riot in 1983, which human rights groups say killed 2,000 Tamils. Some 600,000 went to western countries and 100,000 to India. The UNHCR said that more than 180,000 Sri Lankans who were displaced within the country have returned home since the ceasefire, while around 1,000 refugees have already returned from India (Source: Daily News, 16 Jan 2003).

## Note 10.1 Monetary Policy and Evidence of substantial inflation inertia:

The CBSL, remains not fully independent from the government (the Secretary of the Treasury is a member of the Monetary Board and the MLA allows the Minister of Finance to direct the CBSL to adopt certain policies). To achieve its objectives, the CBSL monetary program targets the rate of growth of reserve money. In particular, the CBSL has aimed, indirectly, at a rate of expansion of broad money in line with expected growth in nominal GDP. As the money multiplier has remained broadly unchanged in recent years (after accounting for changes in reserve requirements), this has translated into a similar target for reserve money growth.

## 10.2 Monetary Policy Transmission Mechanism

The CBSL relies mostly on the interest rate and credit channels for the transmission of monetary policy to rices and output. Thus, a drop in policy rates is expected to lead to a decline in market-determined interest rates and to an increase in lending that would in turn have a positive effect on economic activity while putting upward pressure on inflation. Alternatively, one can put this story in terms of money: if the CBSL engineers an (unexpected) expansion of the money supply, activity and prices will tend to rise.

## 10.3 Evidence of Substantial Inflation Inertia

A shock to inflation generates a substantial further increase in prices for more than two years. Wage formation in the government sector, which in the past has been strongly backward looking, coupled with a central bank that has been willing to accommodate high inflation expectations are a probable cause for inflation inertia. *(Source: IMF Country Report No. 04/69, Sri Lanka: Selected Issues and Statistical Appendix, March 2004).*

## Note 11: Sri Lanka - A Rough Estimate of Charges Payable by Workers Going for Foreign Employment

| Employment Category | Charges approved by SLBFE per worker in SLR | Informal Charges* in SLR |
|---|---|---|
| 1. Household worker | 13,500 | 50,000-65,000 |
| 2. Technical worker/Assistant Accountants | 13,500 | 150,000-185,000 |
| 3. Heavy duty vehicle driver | 13,500 | 150,000-175,000 |
| 4. Miscellaneous workers | 13,500 | 100,000- 125,000 |
| 5. Accountant | 13,500 | 200,000-300,000 |

*Source: Interviews with potential workers and SLBFE officials.*

*Notes: 1. *this is about 3 months salary in SLRs.*

2. *these are rough estimates based on salaries quoted in advertisements and information given by potential foreign workers who have gone for interviews.*

3. *the employment agents are required to collect their recruitment costs from foreign employers; however only a few comply with this SLBFE requirement.*

## Note 12: Non Resident Foreign Currency (NRFC) Accounts

- Applicants must be employed abroad or within 90 days of return to Sri Lanka.
- Sri Lankans living abroad with foreign citizenship are also eligible.

## Benefits

- Higher interest rate on your foreign earnings.
- Interest credited in account currency.
- NRFC funds are freely transferable without being subject to exchange control regulations.
- Transactions can be made in any of accepted currencies.
- No commission is charged for crediting inward remittances to NRFC account.
- A free Life Insurance Cover of up to Rs.1 million for account holders depending on the balance maintained in the account.
- A housing loan at a lower rate of interest.
- Loans to commence own business at a low rate of interest.
- International VISA Credit Card facilities on the strength of NRFC Account balance.
- Rupee loans and overdrafts can be obtained up to 90% against NRFC balances at concessional rates of interest.
- NRFC deposits are exempted from Income Tax.

(2) NRFC Accounts can be opened in,

- US Dollars, Singapore Dollars, Canadian Dollars, Sterling Pounds
- Australian Dollars, Euro and Swiss Francs

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## Appendices

### Table A1: Key Economic Indicators

| Indicator | Y2001 | Y2004 | Y2005 |
|---|---|---|---|
| 1. Population( In Mns) | 18.7 | 19.5 | 19.7 |
| 2. Unemployment rate | 7.9 | 8.3 | 7.7 |
| 3. Percapita GDP (in US$) | 841 | 1030 | 2366 |
| 4. GDP growth rate | -1.5 | 5.4 | 6.0 |
| 5. Inflation Rate (CCPI) | 14.2 | 7.6 | 11.6 |
| 6. Exchange rate(SLR / US $ ) | 93.16 | 104.6 | 102.12 |
| 7. Interest Rate- Com Banks 12 month FD | 14.5 | 9.8 | 11.5 |
| 8. No of International banks licenced to engage in forex transactions | 11 | 11 | 11 |
| 8. 1 Branches and outlets | | 33 | 37 |
| 9. No of domestic banks licensed to engage in forex transactions* | 12 | 12 | 12 |
| 9.1 Domestic branches* | | 1453 | 1482 |
| 10. ATMs per 100,000 persons | 3.3 | .. | 4.25 |
| 11. Banking density( no of bank branches per 100,000 persons) | 6.1 | .. | 7.3 |

Note: *Including National Savings Bank *Source: CBSL Annual* Reports

### Table A2: Sri Lanka -Worker Remittances by region/country

| Origin | Y2001 In US $ mn. | Y2005 In US $ mn. | Y2001 In SLR mn | Y2005 In SLR mn | % 2001 | % 2005 |
|---|---|---|---|---|---|---|
| 1. Middle East | 703 | 1089 | 62,680 | 111,179 | 60.8 | 56.8 |
| 2. North America | 81 | 125 | 7,022 | 12,732 | 7.0 | 6.5 |
| 3. South & Central America | 12 | 19 | 1,042 | 1,941 | 1.0 | 1.0 |
| 4. European Union | 190 | 335 | 14,045 | 35,914 | 15.5 | 18.5 |
| 5. Eastern Europe | 4 | 10 | 381 | 971 | 0.4 | 0.5 |
| 6. Europe other | 60 | 125 | 5,198 | 12,618 | 5.2 | 6.5 |
| 7. South Asia | 7 | 19 | 603 | 1,941 | 0.6 | 1.0 |
| 8. South East Asia | 22 | 38 | 1,905 | 3,883 | 1.9 | 2.0 |
| 9. Far East Asia | 61 | 86 | 5,353 | 8,736 | 5.3 | 4.5 |
| 10. Australia | 14 | 29 | 1,201 | 2,912 | 1.2 | 1.5 |
| 11. Other | 11 | 24 | 996 | 2,427 | 1.0 | 1.5 |
| Total | 1,155 | 1,918 | 103,180 | 21,619 | 100 | 100 |

*Source: CBSL, Annual Reports*

### A3. Sri Lanka- Worker Remittances in 2004-(data for chart in %)

| | |
|---|---|
| 1. Bank of Ceylon | 56.4 |
| 2. Peoples Bank | 19.0 |
| 3. Seylan Bank | 9.4 |
| 4. Commercial Bank | 6.4 |
| 5. Hatton National Bank | 5.2 |
| 6. Sampath Bank | 4.9 |
| 7. Others | 3.3 |
| 8. Total | 100. |

*Source: Table 2 in the text*

Table A4: Sri Lanka- Financial Institutions not authorized to engage in receiving foreign remittances

| Category of Financial Institution | Head office and branches | Remark |
|---|---|---|
| 1. Licensed Specialized Banks(LSB) | 13 (HO) | Licensed and supervised by CBSL |
| Regional Development Banks | 197 | Licensed and supervised by CBSL |
| Private saving banks | 20 | Licensed and supervised by CBSL |
| 2. Finance companies | 128 | Licensed and supervised by CBSL |
| 3. Coopertive Rural Banks(CRBs) | 1400* | Registered with CDD |
| 3.1 Thrift and Credit Co-Operative Societies | 500* | Registered with CDD |
| 4. Samurdhi Bank Societies (SBS) | 1037 | State owned MFIs |
| 5. NGO MFIs | 300* | Not licensed to accept deposits |

*Source: CBSL and other sources*

*Notes: * estimate of active ones, CCD=Com. of Cooperative Development*