

### **Red Flags in Transaction Due Diligence**

Conducting comprehensive due diligence analysis prior to entering in a domestic or international transaction is critical to a successful risk management strategy for trade. Stated simply, U.S. law specifically prohibits any person or business entity in the U.S. to enter into a business transaction or “trade” with any other person or entity if there is any reason to believe that other person or entity is considered a threat to national security. The process of discerning the legitimacy of parties to, and terms of, a business transaction is known as Transaction Due Diligence.

When performing transaction due diligence, encountering information that seems inconsistent or abnormal for the given circumstances is referred to as a “Red Flag.” In general, Red Flags are anything that gives you pause or raises concern about the legitimacy of the person or entity with which you are considering engaging.

Red Flag detection, as with all transaction due diligence reviews, must be conducted PRIOR to entering into a business transaction and should also be repeated at any point where a new party or country is introduced into the transaction. Red Flags may be detected, however, at any point during a transaction. When Red Flags are raised, it is important to exercise due diligence to review the circumstances and determine if the transaction can proceed, should be held for further review, or be suspended to prevent engaging in a prohibited transaction or with a prohibited party.

Although not exhaustive, the following list highlights some examples of common circumstances that should raise suspicion in a transaction. These examples may or may not be indicative of a Red Flag for a particular transaction. It is the responsibility of the U.S. party considering the transaction to look at any aspect particular to that transaction to determine the legitimacy of the terms and parties involved. This is particularly important when the other entity is unknown to you or your company.

Additional information about transaction due diligence is also available in Torres Law’s Practice Guide ***Transaction Due Diligence*** available in the Mondaq Advice Centre.

- The same or similar entity name or address is found on any of the U.S. government watchlists
  - See Torres Law’s ***Guide to Denied Party Lists*** (available in the Mondaq Advice Centre) for detailed information on publicly-available lists to check
- Unverifiable Addresses
  - Incomplete or untrue address
  - Postal box only address (no physical facility location provided)
  - Inability to locate physical address with internet map search
- Use of webmail email addresses, rather than a business email address
- No company website

- Multiple companies or entities listed at the same address
- Recent company name changes or relocation
- The business sector of the entity seems inconsistent with the type of transaction (Ex: a clothing manufacturer purchasing aircraft parts; or a wine maker purchasing industrial lasers)
- Inquiries from individuals in a generally business-to-business transaction
- The entity is unable or unwilling to provide clear answers to commercial or technical questions that are routine in a business transaction
- Transshipment requested through a country that is considered a risk for diversion or seems geographically unrelated to the entity's country of business
- Unusual payment terms, such as requests to pay in cash, wire transfers to a banking facility in another country, or multiple or unusual sources of funding
- A credit check reveals little or no information about the entity, or information is inconsistent with that provided by entity
- A freight forwarder or broker address is listed as the final destination for shipment
- Standard installation services or training are declined by the purchasing entity in a transaction where those types of services are generally requisite for the item being purchased
- Requests to involve individuals in transactions normally between government entities
- Requests for unusual or excessive confidentiality about the terms of, or the parties to, the transaction
- Unexplained urgency or last minute requests for changes to the transaction
- A trust or private investment company involved in the transaction is unable or unwilling to provide information on controlling parties or beneficiaries
- Inquiries made outside of normal business channels
- Requests for unusual labeling or packing for shipment of goods
- Requests for specific stated values on customs documents
- Requests to subvert normal or required recordkeeping procedures