



By Email ([aml\\_consultation@fstb.gov.hk](mailto:aml_consultation@fstb.gov.hk)) and By Hand

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Division 5, Financial Services Branch  
Financial Services and the Treasury Bureau  
24/F, Central Government Offices  
Tim Mei Avenue, Tamar  
Central  
Hong Kong

Dear Sirs,

**Enhancing Anti-Money Laundering Regulation of Designated Non-Financial Businesses and Professions**

The Hong Kong Institute of Certified Public Accountants ("the Institute") has considered the proposals in the consultation paper, "*Enhancing Anti-Money Laundering Regulation of Designated Non-Financial Business and Professions*". Broadly, we support the introduction of legislation on customer due diligence ("CDD") and record-keeping ("RK") for the so-called "designated non-financial business and professions ('DNFBPs') under the Financial Action Task Force ("FATF")'s Recommendations on anti-money laundering/ combating the financing of terrorism ("AML"). We understand that the FATF requires that its members, which include Hong Kong, codify the CDD and RK requirements, as well as suspicious transaction reporting, in the law. As Hong Kong is scheduled to undergo an FATF mutual evaluation in 2018, this has become more urgent.

We believe that it would be preferable to have dedicated legislation that is more tailored towards the needs of DNFBPs rather than trying to extend the scope of the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance (Cap. 615)("AMLO"), which, as the name suggests, was drawn up with financial institutions in mind and is couched in terms of financial institutions ("FIs"). However, we appreciate that a similar problem of language is inherent in the FATF Recommendations, which were conceived from the standpoint of banks and other FIs and only later extended to DNFBPs, without any review of the language or concepts embedded in them. We also consider that it would be better to allow more lead time for discussion of the process of bringing DNFBPs within the statutory framework. Nevertheless, while the current approach may not be ideal, it may be workable if it is carefully thought out and implemented. In this regard, we would urge the government to work closely with the DNFBP sectors during the drafting of the legislation.

Before providing our comments on the specific questions listed in Part 4 of the consultation paper, it may be useful to outline briefly the Institute's existing regulatory authority and powers in relation to its members ("CPAs") and member practices ("CPA practices") and relate these to certain issues that we have identified in the proposals contained in the consultation paper.

**Regulatory authority**

The Institute is the licensing body for CPAs in Hong Kong under the Professional Accountants Ordinance (Cap. 50)("PAO") and is responsible for regulating the conduct of CPAs. As part of its regulatory function, the Institute addresses complaints concerning the ethical and professional conduct of CPAs, CPA practices and registered students.

Compliance with the Institute's professional standards is a requirement of membership. The complaint and disciplinary processes are key mechanisms by which the Institute regulates the



conduct of its members, with sanctions potentially being imposed for serious breaches of professional standards.

Members of the Institute have the knowledge to provide a wide range of professional services to their clients. Currently, it is a requirement that auditors who sign audited financial statements in Hong Kong must be practising CPAs (i.e., hold a practising certificate issued by the Institute). This requirement does not apply to other services offered by CPA practices, e.g., accounting, advisory, cash management, company secretarial and tax, and owners of CPA practices may offer such services via related, but separate legal entities. Therefore, if CPAs or other providers supply services, aside from auditing, via separate legal entities, the Institute does not have specific regulatory authority over these activities or entities.

However, the Institute has authority over the general conduct of individual CPAs. Accordingly, if a complaint is lodged against a CPA working in such an entity, the Institute has the authority to handle the complaint according to its statutory complaint procedures.

Section 34 of the PAO sets out the complaint procedure and grounds for complaints against CPAs and CPA practices, and section 35 sets out the possible sanctions that may be imposed by a disciplinary committee if a complaint is upheld. In addition, various criminal offences are prescribed in section 42, including offences relating to falsely holding oneself out to be a CPA or a CPA (practising).

As indicated in the Institute's Compliance Operations Report 2015, a majority of the cases handled by the Compliance Department of the Institute were related to section 34 of the PAO. If a complaint is substantiated, depending on the gravity of the matter, a range of possible sanctions may be imposed, including:

- reprimand;
- financial penalty;
- cancellation of practising certificate;
- removal from the membership register on a temporary or permanent basis; or
- a combination of the above sanctions.

### **The practice review regime**

The PAO empowers the Institute to conduct practice reviews of CPA practices, in relation to their application of professional standards, primarily auditing standards. Where deficiencies are identified, follow-up action will be taken, there may be subsequent visits and, in serious cases, a complaint can be initiated. Practice review is the only form of active monitoring of CPA practices that the Institute is empowered to carry out under the law.

The Institute's Quality Assurance Department ("QAD") is responsible for the practice review process. The process can be divided into three main stages, namely, (i) preparation; (ii) on-site visit/ in-house desktop review; and (iii) reporting. Matters identified during a review are discussed with the practice management. QAD is responsible for drawing up a report and making recommendations to the Practice Review Committee of the Institute. The Practice Review Committee may decide to initiate disciplinary action against a CPA practice, e.g., if, during the practice review, QAD identify serious violations of the ethical and professional standards, or if a CPA practice takes no action to remedy deficiencies identified by QAD, even after follow-up visits.

If active monitoring of AML compliance in relation to the proposed CDD and RK requirements is expected by the FATF and the Hong Kong SAR Government, then it may be necessary to bring the AML guidelines, envisaged in paragraph 3.20 of the consultation paper, within the scope of practice review, by issuing them as a professional standard, e.g., as an addition to the Code of Ethics for Professional Accountants.



### **Potential regulatory gaps under the proposal**

The consultation paper indicates, at paragraph 3.4(b), that the statutory CDD and RK obligations will apply to accountants and solicitors when they prepare for or carry out transactions for their clients concerning:

- (i) the buying or selling of real estates;
- (ii) managing of client money, securities or other assets;
- (iii) management of bank, saving or securities accounts;
- (iv) organisation of contributions for the creation, operation or management of companies;
- (v) creation, operation or management of legal persons or arrangements; and
- (vi) the buying or selling of business entities.

The above activities are those specified in relation to legal professionals and accountants under FATF Recommendation 22. Under the same FATF Recommendation, a different, albeit in some areas related, set of activities are specified in relation to trust and company service providers ("TCSPs"), which comprise a separate DNFBP sector. These latter activities are essentially the same as those listed in paragraph 3.4(c) of the consultation paper, which are: Preparing for or carrying out transactions for a client concerning:

- (a) the forming of companies or other legal persons;
- (b) acting, or arranging for another person to act, as a director or secretary of a company, a partner of a partnership, or a similar position in relation to other legal persons;
- (c) providing a registered office, business address, correspondence or administrative address or other related services for a company, a partnership or any other legal person or arrangement; and
- (d) acting, or arranging for another person to act, as a trustee of an express trust or similar legal arrangement, or a nominee shareholder for a person other than a company whose securities are listed on a regulated market.

Under the proposals, a licensing regime will be established for TCSPs, which will be administered by the Registrar of Companies ("R of C"). We understand that other regulated DNFBPs, which conduct one or more of the TCSP-type activities, may be exempted from having to obtain a licence so as to avoid regulatory overlaps.

Against the background of the above explanations, we are of the view that there are potential regulatory gaps in the proposals:

- I. Some owners of CPA practices also provide non-audit services, including some of those in (i) – (vi) above via a separate legal entity, rather than through the CPA practice. As indicated above, while the individual CPAs involved will be subject to the Institute's regulatory framework, the entity itself will not be, and the Institute will not be in position to carry out active monitoring of AML compliance in relation to such entities. There are, for example, some entities related to CPA practices that carry out, e.g., payroll services or services related to mergers and acquisitions for their clients, (which could be construed as falling within the services specified in (ii) and (vi) respectively).
- II. If our members provide any of the TCSP-type company services in (a) – (d) through a separate legal entity, the result will be the same as immediately above. Furthermore, if AML guidelines issued by the Institute target the activities specified by FATF for accountants (i.e., those in (i) – (vi) above), then the service providers offering TCSP-type services, even if they are CPA firms, could fall through the net, unless they are regulated by R of C as TCSPs. One option would be for the scope of AML guidelines issued by the Institute to seek to cover the company services in (a) – (d) as well as the specified activities for accountants in (i) – (vi), above. However, this still would not address the gap identified in paragraph I above.

- III. The Institute is the sole body authorised by law to register and grant practising certificates to CPAs in Hong Kong and it is empowered to regulate its own members. However, some overseas accounting bodies operate through branches in Hong Kong (CPA Australia, the Association of Chartered Certified Accountants, the Institute of Chartered Accountants of England and Wales, etc.) and have members working in Hong Kong who may provide professional services, other than auditing, to clients. Some people may be under the impression that "accountants" under the FATF Recommendations would include qualified accountants from other jurisdictions who work in Hong Kong. Therefore, there may be a need to educate the public that these practitioners are not regulated by the Institute and, if they carry out any of the services in (i) – (vi), they may not be regulated for AML in Hong Kong when they do so.

### **Other issues**

A more general concern that we have is that the meaning of phrase "prepare for or carry out transactions for their clients" in paragraph 3.4 of the consultation paper is by no means clear. While this may be language used by the FATF, the government should clarify what, specifically, is intended to be covered by this phrase under Hong Kong law, so that relevant authorities and those that they are regulating are not left in any doubt.

As indicated above, the language of the AMLO is not tailored for the services that non-FIs, in particular accountants, more commonly provide. Therefore, in amending the legislation, it will be important to minimise the risk of ambiguity and to ensure that DNFBPs are not left pondering how to interpret terminology and requirements that may be relevant to the transactional-based services provided by FI, but which have no clear application to accountants. This will be relevant not only to the main provisions of Schedule 2 and other parts of the legislation, but also to the definitions contained in the interpretation sections.

Our comments on the detailed questions in the consultation paper are provided below.

### **Comments to the questions in Section 4 of the consultation paper**

- 4.1 Do you agree with the application of a risk-sensitive approach, whereby the CDD measures to be undertaken by DNFBPs should be commensurate with the risk profiles of customers?**
- 4.2 Do you agree that DNFBPs should be subject to enhanced CDD measures when dealing with customers presenting a high risk of money laundering or terrorist financing?**
- 4.3 Do you think DNFBPs should be allowed the flexibility to undertake simplified CDD measures on low-risk cases, with reference to the list of eligible customers and products as specified in the AMLO?**

This response relates to the above three questions. The proposals form part of a legal framework that Hong Kong has to put in place in order to implement FATF standards on AML. As DNFBPs have a part to play in combating money laundering/ terrorist financing ("ML/ TF") activities, they are expected to conduct proper CDD before entering into business relationships with clients and to conduct ongoing monitoring. However, a balance has to be struck between costs and benefits of AML risk management.

DNFBPs should have in place sound governance arrangements to ensure effective risk management. The board of directors/ senior management of DNFBPs should approve and oversee their policies for AML risk management and compliance. A senior level person, such as a partner or director, with the necessary authority, and good access to the top levels of the entity should be appointed as compliance officer and have overall



responsibility for the AML function and controls.

With the appropriate AML policies, controls and personnel in place, DNFBPs should be able to make the most efficient and effective use of their resources by adopting a risk-based approach ("RBA") in complying with AML requirements. This is encouraged by FATF (see, e.g., Recommendations 1 and 10). FATF has published guidance on an [RBA for accountants](#), which the Institute was invited to comment upon during the drafting stage. Therefore, we support the adoption of a risk-sensitive approach to conducting CDD.

When adopting an RBA in relation to CDD procedures, it is clearly pragmatic and we would agree that enhanced CDD should be applied where clients, services, products, etc. pose a higher ML/TF risk, while simplified CDD may be adopted in relation to clients, services and products carrying a lower than normal risk. Ongoing monitoring is an essential part of an effective CDD procedure. It should also be understood that risk profiles can change over time and that the risk category of particular clients may also change, triggering a corresponding change of the approach towards them. This could entail conducting further CDD in some cases.

Paragraph 3.8 of the consultation paper summarises circumstances where FIs may adopt simplified CDD under the AMLO. Although the list was prepared with FIs in mind, most of the items on it would also appear to be applicable to DNFBPs. Therefore, we would agree in principle that simplified CDD can be deployed by DNFBPs when dealing with clients, services or products contained on the list. However there may also be others, as indicated in our response to question 4.4.

**4.4 Do you think there are other justified additions to the specified list of customers and products eligible for simplified CDD treatment under the AMLO by DNFBPs? If so, what are they; and what are the justifications?**

The specified list of customers and products eligible for simplified CDD treatment in paragraph 3.8 has been drawn up with FIs in mind. Accountants do not usually handle clients' money, as FIs and some DNFBPs may do, so the considerations may be different. As DNFBPs come from different professional and industry sectors, and the risks faced by each sector will not necessarily be the same, a one-size-fits-all approach would not be appropriate. As it is proposed that relevant professional bodies/authorities in different DNFBP sectors will be responsible for overseeing AML compliance within their areas, and as they should have an extensive knowledge of their own sectors, these bodies/authorities should be given flexibility to expand the list of items eligible for simplified CDD treatment for their own sectors in the guidelines that they issue.

One additional category of entities that should be included on the list as part of the current package of proposals is other DNFBPs regulated for AML, when they are acting as clients of a DNFBP.

**4.5 Do you agree that DNFBPs should be subject to a six-year record-keeping requirement on a par with financial institutions?**

According to FATF Recommendation 11, records should be kept for a minimum of five years. While a six-year RK requirement would be consistent with the existing obligation on FIs under AMLO, we see no strong reason to go beyond the FATF minimum standard. Auditing standards also set a retention period for documentation of a minimum of five years. Consistency in the RK requirement under the AMLO is preferable, so we would suggest that consideration be given to setting a minimum retention period of five years across the board, even though that may mean amending the existing requirement applicable to FIs.



- 4.6 Do you agree with the proposed designation of the respective regulatory authority for solicitors, accountants, real estate agents and TCSPs?**
- 4.7 Do you agree that, instead of introducing one new single regulatory body for solicitors, accountants and estate agents, the prevailing investigation, disciplinary and appeal mechanisms under the respective governing Ordinances of the professions should be relied upon to enforce the statutory CDD and record keeping requirements?**

This response relates to the above two questions. The relevant professional bodies have a wide knowledge of their own sectors and extensive experience of regulating their members. It makes sense to give them the authority under AMLO to supervise their members for AML compliance with the proposed statutory CDD and RK requirements, using their existing disciplinary frameworks. This is the approach adopted in the United Kingdom and various other jurisdictions overseas. As regards the accounting profession, the Institute has a robust and efficient regulatory framework to govern the professional conduct of its members. The disciplinary procedures are backed by the PAO and are conducted on a fair and reasonable basis. We are of the view that the Institute's existing investigation, disciplinary and appeal mechanisms under the PAO could be relied upon for enforcement of the statutory CDD and RK requirements.

Setting up new AML regulatory agency, on the other hand, to supervise quite diverse DNFBP sectors for AML compliance, would be a costly and cumbersome approach.

- 4.8 Do you consider it necessary to introduce new criminal sanctions for non-compliance with the statutory CDD and record-keeping requirements under the AMLO by DNFBPs?**

Taking into account the implications of non-compliance with statutory CDD and RK requirements and the scope of the Institute's disciplinary arrangements, we believe that the existing regulatory sanctions should be dissuasive and proportionate to deal with any non-compliance by members of the profession. The Institute's disciplinary powers extend to, for example, the striking off of a CPA practice or a CPA from the register, either for a certain period or permanently. Sanctions such as these, coupled with the loss of reputation, are very serious for professionals and should provide an effective deterrent. There should be no need to introduce additional criminal sanctions.

- 4.9 Do you think that the Law Society, the HKICPA and the EAA should be given inspection and search powers similar to those available to AML regulatory authorities for financial institutions under Part 3 of the AMLO?**

The Institute's regular practice review procedure already allows the practice reviewers to visit CPA practices and to examine records to see how they have applied auditing and other standards. We believe that these powers should, in principle, be sufficient to monitor the AML compliance of CPA practices.

Furthermore, as indicated above, CPA practices and CPAs do not usually handle client monies and do not engage widely in the FATF-specified activities. Broadly speaking, the ML/ TF risks facing by accountants are relatively low compared with FIs and professionals who may regularly handle client monies.

Under the circumstances, we do not see the need to call for additional inspection and search powers.

**4.10 Do you agree with the provision of a 90-day transitional period for existing TCSP operators to migrate to the new licensing regime?**

We consider that a 90-day transitional period for existing TCSP operators to migrate to the new licensing regime is too short. This is a sector that has not been required to be licensed and has been virtually unregulated up until now and, to our knowledge, there has been little discussion about regulating the TCSP sector other than in the context of introducing an AML framework for DNFBPs. There may be many entities operating in this area, particularly given Hong Kong's role as a commercial centre and entrepot, and its long established connections with offshore jurisdictions. In view of the practical issues, we suggest that a longer transitional period of, at least, 180 days would be more appropriate. It will also be essential that R of C has sufficient resources to deal with the anticipated volume of work, as expeditiously as possible.

**4.11 Do you think the criteria for determining the fitness and properness of TCSPs appropriate? If not, what criteria should be included or excluded?**

Under the current proposal, the criminal and bankruptcy records of the applicant (for natural persons), any ultimate owners, or the partners/directors/shareholders (in cases of partnerships/ legal persons), and where the applicant is a corporation, whether it is in liquidation or receivership, as well as any failure to comply with the requirements under the AMLO and guidelines to be issued by the R of C, will be the key considerations for determining the fitness and properness of TCSPs. However, it is not entirely clear how these factors will be applied. We would assume, for example, that a past bankruptcy on the part of an individual would not be a bar to obtaining a licence, but that has not been spelled out.

Generally speaking, professional bodies in Hong Kong already have in place quite stringent "fit and proper persons" tests and we would suggest that there be a level playing field under the proposed licensing regime for TCSPs. The test for TCSPs should, as far as possible, be aligned with those for the professions. We would suggest that, where they may need to obtain a TCSP licence, members of professional bodies which already apply "fit and proper" criteria should be granted an exemption from the proposed fit and proper test to be applied by R of C. At the same time, they should be required to inform R of C, in a timely manner, of any significant changes that may affect their status, including, potentially, whether they are under investigation in relation to a serious complaint against them.

Licensed persons generally should be required to inform the R of C of any significant changes that may affect their fit and proper status in a timely manner. In addition, the test should be refreshed upon renewal of a licence.

**4.12 Do you agree with the three-year validity of a TCSP license (renewable on application)? If not, what should be the validity period?**

A three-year validity period for a TCSP licence, with the licence being renewable on application, would seem to be reasonable.

**4.13 Do you agree that any persons operating TCSP business without a valid licence should be liable to criminal sanctions (including a fine at level 6 and/or imprisonment of up to six months)?**

It would be expected that persons operating a TCSP business without a valid licence could face criminal sanctions. We understand that the proposed sanctions are comparable to those applicable to money service operators under the AMLO. As indicated above, there are criminal penalties in section 42 of the PAO in relation to, for



example, persons falsely claiming to be qualified to provide services as a CPA practising or a CPA practice. However, the levels of penalties under the PAO differ from those proposed. The maximum penalty on individuals under section 42 of the PAO is a fine at level 4 and imprisonment of up to 12 months. For the sake of consistency, it may be worthwhile to try to harmonise the penalties for similar offences in the various ordinances relating to DNFBPs.

**4.14 Do you agree with the proposed supervisory sanctions for TCSPs in respect of non-compliance with statutory CDD and record-keeping requirements?**

The proposed supervisory sanctions for TCSPs, in respect of non-compliance with statutory CDD and RK requirements, are on a par with those contained in the PAO and would seem to be appropriate.

**4.15 Do you agree with the re-constitution of the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Review Tribunal to cover appeals against future decisions of the Registrar of Companies in respect of the licensing and disciplinary regime for TCSPs?**

There should be an appeal mechanism to cover decisions made by the R of C in respect of the TCSP licensing and disciplinary processes, so it makes sense to expand the remit of the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Review Tribunal. It should be made clear, however, that the scope of the Review Tribunal will not cover decisions made by professional bodies designated as relevant authorities under AMLO, as their existing appeal mechanisms will continue to apply to appeals by their members against decisions of the professional body.

**4.16 Do you agree that the threshold for determining controlling interest of beneficial ownership under the AMLO should be revised from not less than 10% to more than 25%, to align with the future requirement under the Companies Ordinance?**

We support the proposed amendment to the threshold for determining controlling interest of beneficial ownership under the AMLO, from not less than 10% to more than 25%. The latter is the threshold given as an example by the FATF in the interpretative note to Recommendation 10 and we understand that it is the threshold adopted quite widely internationally. It also aligns with the proposed threshold in the concurrent consultation proposals on enhancing the transparency of beneficial ownership of Hong Kong companies.

Should you have any questions on our submission, please feel free to contact me on 2287 7084 or by email at [peter@hkicpa.org.hk](mailto:peter@hkicpa.org.hk).

Yours faithfully,

Peter Tisman  
Director, Advocacy and Practice Development

PMT/EKC/sf