

CONSULTATION CONCLUSIONS – FIRST-ROUND CONSULTATION

Introduction

A.1 FSTB published a consultation paper on 9 July 2009 on a conceptual framework of a legislative proposal to enhance AML regulatory regime in respect of the financial sectors.

A.2 The proposed legislation seeks to address the deficiencies identified by FATF in the Hong Kong's AML regime. The conceptual framework of the legislation covers the following aspects:

- the financial institutions which would be subject to the proposed legislation;
- the customer due diligence (CDD) and record-keeping obligations that are required to be met;
- the powers of the regulatory authorities in supervising compliance with appropriate checks on the exercise of such powers;
- criminal and supervisory sanctions for breaches of the obligations; and
- a proposed licensing system applicable to entities engaging in remittance and money changing services for AML regulatory purpose.

A.3 The consultation period closed on 8 October 2009. Apart from the feedback we received through the seven sectoral consultative sessions which were attended by over 800 participants, we also received a total of 39 written responses to the consultation paper. Written responses are received from:

- Almighty Global Company
- Cheetah Investment Management Limited
- Clifford Chance
- David Ross
- Eddie S CHAN
- Global Witness
- Hong Kong Bar Association
- Hong Kong General Chamber of Commerce
- Hong Kong Investment Funds Association
- Hong Kong Securities Association
- Hong Kong Securities Professionals Association
- Hong Kong Trustees' Association (HKTA)

- ING Life Insurance Company (Bermuda) Limited
- Institute of Financial Planners of Hong Kong
- Ipac Financial Planning Hong Kong Limited
- Kelvin Ng
- Macquarie Services (Hong Kong) Limited
- R S Nair (Lotus Forex Limited)
- National Australia Bank (Hong Kong Branch)
- Optiver Trading Hong Kong Limited
- Retirement Scheme Subcommittee of HKTA
- Rodelo B Landicho
- Securities and Futures Commission Advisory Committee
- SmarTone Mobile Communication Ltd
- STEP Hong Kong Limited
- The Alternative Investment Management Association Ltd
- The Association of Remittance Agents and Money Changers
- The Deposit-taking Association
- The Hong Kong Association of Banks
- The Hong Kong Confederation of Insurance Brokers
- The Hong Kong Federation of Insurers
- The Law Society of Hong Kong
- TMF Group
- Travelex Hong Kong Ltd
- 謝健全、施金定

(Two respondents requested not to disclose their identity and there are two anonymous response)

Views and Comments

A.4 The comments received in the previous consultation are generally positive. Many respondents acknowledged the need for Hong Kong to comply with the international AML standards which was important for maintaining our status as an international financial centre. There was broad support for the Government's proposal to introduce legislation to enhance the AML regulation and introduce a licensing regime for RAMCs. Major views by topics with Government's response are summarized in the Appendix.

**SUMMARY OF MAJOR COMMENTS RECEIVED WITH THE
ADMINISTRATION’S RESPONSE**

Issues	Comments Received	Response from the Administration
Need for Legislation	<ul style="list-style-type: none"> • A number of respondents recognized the need for Hong Kong to meet the international obligations to maintain status as an international financial centre. • Some respondents considered it preferable to put the requirements in a regulation (instead of primary legislation) which is more flexible. 	<ul style="list-style-type: none"> • Noted. • We propose that the detailed CDD and record-keeping requirements be set out in a schedule to the proposed legislation. In case there are changes to the international standards which require amendments to the proposed legislation, Secretary for Financial Services and the Treasury (SFST) may amend the schedule by notice in Gazette which is subject to negative vetting by the Legislative Council.
Governing Principles	<ul style="list-style-type: none"> • A number of respondents supported the principle that impacts on the relevant financial sectors should be minimized as far as reasonably practicable, whilst one respondent considered that compliance cost is not relevant as the key is to comply with international requirements. • Some respondents asked that the obligations under the proposed legislation be proportionate to the Financial Action Task Force (FATF)’s requirements and be 	<ul style="list-style-type: none"> • Noted. • Noted.

	<p>benchmarked against other competent international financial centres to maintain competitiveness, and not to impose additional onus and/or burden on daily business operations especially of those smaller establishments.</p> <ul style="list-style-type: none"> • Some respondents commented that the proposal should be consistent with Personal Data (Privacy) Ordinance. 	<ul style="list-style-type: none"> • We will seek Privacy Commissioner’s advice, as appropriate, in preparing the legislation.
Coverage	<ul style="list-style-type: none"> • A few respondents suggested that the new legislation should not apply to the following categories of financial institutions (FIs): <ul style="list-style-type: none"> (a) Type 6 licensed corporations advising on corporate finance (b) Market makers (proprietary traders) (c) Reinsurance companies authorized under Insurance Companies Ordinance, Cap. 41 (ICO) • Some respondents pointed out that some businesses carrying out similar activities and are not regulated by the financial regulators yet (e.g. credit card issuers and money lenders) are not covered in the proposed legislation. 	<ul style="list-style-type: none"> • According to FATF’s requirements, these categories of FIs are not exempted from the customer due diligence (CDD) and record-keeping requirements. • FATF’s last evaluation on Hong Kong in 2008 acknowledged that the impact of excluding money lenders and other peripheral financial activities from our anti-money laundering (AML) regime on Hong Kong’s overall compliance should be “minimal”. Separately, we will collate information and data on these sectors with a view to assessing

		<p>the money laundering risks involved in these sectors.</p>
<p>Third-party reliance and regulation of Designated Non-Financial Business and Professions (DNFBPs)</p>	<ul style="list-style-type: none"> • A number of respondents suggested that FIs should be allowed to rely on local third parties to conduct CDD, which is a common business practice for financial services. On the other hand, a respondent considered that the reliance on third parties should be tightened up. • Some respondents asked whether lawyers, accountants and trust service providers in Hong Kong can be relied on for CDD, given that they are not regulated for AML purpose at the moment, and some respondents suggested that the regulators should provide clear guidance and criteria on the eligibility of third parties to be relied upon. • Some participants asked whether, for hedge funds that are regulated in another financial centre, FIs would be allowed to rely on them for conducting CDD measures on hedge fund clients. • Some respondents suggested that insurers should be allowed to rely on banks to conduct CDD for bancassurance. 	<ul style="list-style-type: none"> • Taking into account the existing arrangement, we propose to allow FIs to rely on local third parties for CDD under specified circumstances. (See item 10 of the detailed legislative proposals) • The relevant eligibility criteria are set out in item 10(e) of the detailed legislative proposals. • Yes, if the hedge funds satisfy the criteria set out under item 10(e) of the detailed legislative proposals. • It would depend on the nature of the agreement between the banks and the insurers. Generally speaking, banks covered by the new legislation can be relied upon in conducting CDD, although the insurers would still be ultimately responsible for the CDD. (See

	<ul style="list-style-type: none"> Although outside the scope of this consultation, it is noted that some respondents commented that there should be AML regulation of DNFBPs to ensure a comprehensive AML regime, and some industry associations commented that they are willing to come under AML regulation. 	<p>item 10 of the detailed legislative proposals)</p> <ul style="list-style-type: none"> Noted. The views were relayed to the Security Bureau which is responsible for AML regulation of DNFBPs.
Designation of Regulators	<ul style="list-style-type: none"> Most of the respondents agreed to the proposed designation of regulators viz. Hong Kong Monetary Authority (HKMA), Securities and Futures Commission (SFC), Insurance Authority (IA) and Customs and Excise Department (C&ED). A few respondents commented on the appropriateness of designating C&ED as the regulator for remittance agents and money changers (RAMCs). 	<ul style="list-style-type: none"> It is appropriate for C&ED to take up the AML regulatory role for RAMCs, in view of its rich experience and expertise in law enforcement and conducting compliance inspection in trade and industry sectors. Resources and appropriate trainings on AML regulation will be provided to C&ED officers before commencement of the new legislation.
Regulatory Approach	<ul style="list-style-type: none"> A number of participants of the consultative sessions for the banking sector suggested the single-regulator approach and requested that a high level of consistency in the enforcement by regulators should be maintained. 	<ul style="list-style-type: none"> AML compliance interlinks with the overall risk management and control systems of FIs and hence should best be supervised by the same regulators who are overseeing the prudential and/or statutory regulation of these sectors. The designated authorities will seek to enhance consistency in compliance requirements and enforcement standards, and synchronize their

		AML regulatory guidelines and enforcement guidance.
AML Guidelines	<ul style="list-style-type: none"> • Many respondents requested that the AML guidelines underpinning the implementation of the future statutory requirements should be consistent to ensure level playing field for all sectors, but on the other hand some respondents commented that the specific business characteristics of each sector should be taken into account in determining their obligations and the guidelines. • Many respondents supported a risk-based approach, whilst some respondents commented that since non-compliance would in future attract criminal liability, detailed and prescriptive guidelines should be provided by the regulators and aspects requiring FIs to exercise judgment and discretion should be minimized as far as possible. 	<ul style="list-style-type: none"> • Please see our response under “regulatory approach”. • Relevant authorities will provide appropriate guidance in their guidelines to be issued.
CDD requirements	<ul style="list-style-type: none"> • Some respondents enquired the definition of beneficial owners under the future legislation and suggested that the threshold for beneficial ownership should be increased from 10% to 25%. • Some respondents suggested to relax 	<ul style="list-style-type: none"> • We propose to model on the current requirement under the guidelines issued by HKMA, SFC and IA, having regard to the risk associated with the use of offshore corporate vehicles and the satisfactory compliance record thus far, and adopt the existing 10% threshold for beneficial ownership. • Ongoing due diligence is a FATF

	<p>the requirement for ongoing due diligence or apply this obligation only to new accounts. Some respondents suggested that a grace period of at least 12 months should be allowed for FIs to tackle their existing accounts, while a respondent suggested that records of existing customers should only need to be brought up to current CDD standards upon a triggering event.</p> <ul style="list-style-type: none"> • Questions were raised by some respondents from the banking sector on whether local FIs should keep records on those transactions booked overseas and conduct the CDD on such clients. • Different views were expressed on whether the proposed threshold for occasional transactions of EUR/USD 15,000 is appropriate. 	<p>requirement. Exempting all existing accounts for CDD measures will undermine the effectiveness of AML regime. We propose that FIs should review/update existing accounts upon a triggering event. To allow time for FIs to review and update all existing accounts, we propose to provide a transitional period of 2 years. (See item 7 of the detailed legislative proposals)</p> <ul style="list-style-type: none"> • We propose that when the Hong Kong branch conducts a transaction above the HK\$120,000 threshold on behalf of a customer with an account booked in an overseas branch, CDD measures would be required. • The proposed threshold of HK\$120,000 (EURO/US\$15,000) is already the maximum threshold permitted by FATF for occasional transactions. FIs may set a lower (i.e. more stringent) threshold under their own internal policies having regard to the risks associated with their own businesses.
Requirements for RAMCs	<ul style="list-style-type: none"> • Different views were expressed on whether the current threshold (HK\$8,000) for verification of customers' identity is appropriate. 	<ul style="list-style-type: none"> • We propose to maintain the existing HK\$8,000 threshold for wire transfers and remittances and to raise the threshold for money changing transactions to HK\$120,000. (See items 3(c), 13

	<ul style="list-style-type: none"> • A number of respondents expressed concerns that RAMCs may have difficulties in complying with the proposed CDD requirements. 	<p>and 14 of the detailed legislative proposals) These are the maximum levels permitted by FATF.</p> <ul style="list-style-type: none"> • To ensure integrity of new AML regime, RAMCs will be subject to the same requirements as other FIs. The licensing authority will provide training and other necessary technical assistance to RAMCs to help them familiarize with the statutory requirements and facilitate their compliance.
Risk-based approach	<ul style="list-style-type: none"> • Most respondents supported the adoption of a risk-based approach, but they also commented that there should be clear guidelines on how to apply a risk-based approach. • Some respondents stated that there is a need for formal procedures for periodic appraisal and review of risks if a risk-based approach is applied. 	<ul style="list-style-type: none"> • Noted • FIs will be required to apply ongoing due diligence measures by scrutinizing transactions and reviewing existing records. (See item 6 of the detailed legislative proposals)
Enhanced Due Diligence	<ul style="list-style-type: none"> • Many respondents expressed difficulties in identifying high-risk customers, e.g. Politically Exposed Persons (PEPs). Some asked for clear and detailed requirements and an exhaustive PEP list covering all jurisdictions from the regulators or Government. 	<ul style="list-style-type: none"> • The definition of PEPs is set out at the “List of Definitions” in the detailed legislative proposals. It is not a common international practice for relevant authorities to provide exhaustive lists on PEPs. The regulators will provide guidance to FIs though their guidelines to help FIs to conduct PEP checks.

	<ul style="list-style-type: none"> Some respondents considered that enhanced due diligence should not be required for non face-to-face customers (especially those involving credit cards, personal loan or telemarketing), and cross-border correspondence banking relationship which is considered to be of higher risk could be narrowed down to those incorporated in high-risk jurisdictions. 	<ul style="list-style-type: none"> Non face-to-face transactions and correspondent banking relationship are regarded as high-risk customers or transactions under FATF's requirements. There is no scope for provision of exemption for these categories of customers from enhanced due diligence.
Simplified Due Diligence	<ul style="list-style-type: none"> Some respondents suggested that the following financial products should be eligible for simplified due diligence, regardless of the risk profile of the customers: <ul style="list-style-type: none"> (a) MPF products; (b) products which involved no cash benefits; and (c) protection type insurance products with sum insured of less than \$100,000. 	<ul style="list-style-type: none"> Item 8 of the detailed legislative proposals sets out types of customers and products eligible for simplified due diligence.
Regulators' powers	<ul style="list-style-type: none"> Respondents generally supported the proposals on regulators' powers, although there were concerns about whether there would be proper safeguards to ensure that regulators' exercise their regulatory powers properly. 	<ul style="list-style-type: none"> There will be appropriate safeguards in the detailed legislative proposals.
Supervisory Sanctions	<ul style="list-style-type: none"> Most respondents agreed that supervisory sanctions are effective tools to ensure compliance. A few respondents disagreed with the provision of supervisory sanctions as 	<ul style="list-style-type: none"> Supervisory sanctions are particularly effective for dealing with non-compliance of less severity. The proposed legislation will empower the

	<p>criminal sanctions alone would suffice.</p> <ul style="list-style-type: none"> • Some respondents agreed that the maximum fines can be the same as that under s194 of SFO, whilst some commented that a cap in an absolute amount may not fit all sectors. • Questions were raised as to how the authorities would determine whether to apply criminal and/or supervisory sanctions. Some considered that there should not be concurrent imposition of criminal and supervisory sanctions. 	<p>relevant authorities to impose a range of supervisory sanctions upon breaches of the statutory requirements.</p> <ul style="list-style-type: none"> • The legislation will only specify the maximum level of fines that may be imposed. The exact level of fines to be imposed for each case will be determined on a case-by-case basis having regard to all relevant factors. • Under the proposed AML regulatory regime, the regulatory authorities are empowered to investigate suspected breaches of the statutory CDD and record-keeping requirements. The regulator will, upon completion of the investigation, decide whether (a) to prosecute summarily the regulatee for the offence committed or refer to the Director of Public Prosecution for prosecution on indictment; and/or (b) to take actions to impose supervisory sanctions, taking into account relevant factors including the facts of the case, availability of sufficient evidence, and severity and nature of the breach concerned. In any event, as a criminal conviction may also affect the “fitness and properness” of the concerned regulatee, this should not preclude the regulators from imposing any other
--	---	--

	<ul style="list-style-type: none"> • A few respondents commented that considerations for imposing different levels of sanctions should be clearly set out and revocation or suspension of licence should only be imposed upon very serious breach. The rationale for imposing a sanction should be transparent to the FI concerned and made known to other FIs as far as possible. 	<p>appropriate supervisory sanctions.</p> <ul style="list-style-type: none"> • The relevant authorities will publish guidelines on how they intend to use their power to impose supervisory sanctions (See item 35 of the detailed legislative proposals). The relevant authorities may disclose to the public the reason for imposing the sanctions. (See item 36 of the detailed legislative proposals)
<p>Criminal liability for FIs</p>	<ul style="list-style-type: none"> • A few respondents opined that extreme caution should be exercised on introduction of new criminal sanctions. A number of trade bodies as well as a few other respondents considered it not necessary for provision of criminal sanctions for FIs for breaches of CDD and record-keeping requirements. • Some respondents who raised no objection to the provision of criminal sanction suggested that there should be some form of knowledge or intent element for the offence. Some commented that it is unclear what would constitute a “reasonable excuse” against criminal liability, and a statutory defence for criminal liability should be provided, and some suggested to use “enforceable undertakings” (such as the regime under Personal Data (Privacy) Ordinance) in lieu of criminal 	<ul style="list-style-type: none"> • The current proposal is that any persons who knowingly contravene the statutory obligations will commit an offence. (See item 37 of the detailed legislative proposals) • Ditto

	offences.	
Personal Criminal liability	<ul style="list-style-type: none"> Those respondents who raised no objection to personal criminal liability suggested that there should be a high mental threshold and that “officers” should be clearly defined to exclude mid-level executives. Consideration should be given to providing statutory defence such as “reasonable excuse”. On the other hand, some other respondents considered it inappropriate to impose criminal liability on officers. 	<ul style="list-style-type: none"> The current proposal is that only those who knowingly contravene the statutory obligations will commit an offence. Breaches committed out of inadvertence will not be caught. The proposed formulation for criminal liability involves an element of knowledge or fraud. (See item 37 of the detailed legislative proposals)
Compliance Officers	<ul style="list-style-type: none"> Some respondents suggested that the proposed legislation should require FIs to designate AML compliance officers to bear the primary responsibility for AML compliance. One participant of the consultative session suggested to put in place a registration system for frontline staff of FIs to ensure that they possess knowledge on AML requirements. 	<ul style="list-style-type: none"> A compulsory requirement for designation of AML compliance officers may create undue burden to some FIs, particularly those smaller establishments, and imposing a registration system for frontline staff of FIs will have significant impact on industry practitioners.
Transitional Period	<ul style="list-style-type: none"> Most of the respondents suggested that at least 12 months is required to allow time for modification of internal rules and procedures, etc. A respondent suggested that a 2-year period is necessary. Another respondent opined that the obligations can be applicable to new businesses immediately while existing businesses may need 6-12 months for remediation. 	<ul style="list-style-type: none"> The suggestion for a transitional period is noted. The proposed legislation will commence one year after the approval of the bill by the Legislative Council. (See item 61 of the detailed legislative proposals)

RAMC licensing	<ul style="list-style-type: none"> • Most respondents welcomed the licensing regime while a respondent considered the replacement of registration regime with the proposed licensing regime unnecessary. A respondent suggested that only a limited number of licences should be issued to maintain the quality of the industry. • Most respondents have no objection to the need for renewal of licence although some commented that there should be automatic renewal. A respondent commented that renewal should be made at 3 years' interval to avoid undue inconvenience to business operators. 	<ul style="list-style-type: none"> • Market force will determine the size of the RAMC sector. We see no strong policy ground to impose a quota on the number of licences issued. • Taking into account the need to ensure effective supervision and to avoid undue inconvenience to business operations, we propose that RAMC licences should be subject to renewal at two years' intervals. (See item 42 of the detailed legislative proposals)
Licensing Criteria for RAMCs	<ul style="list-style-type: none"> • Suggestions were made that business competence, knowledge of the business and education standards should be included as licensing criteria. A respondent further suggested that both licensees and employees should be required to pass examination. 	<ul style="list-style-type: none"> • The desirability and feasibility of putting in place a trade examination may be considered in the longer run.
Licence Fee for RAMCs	<ul style="list-style-type: none"> • Some respondents considered that a licence fee determined on a cost recovery principle is generally fair, though a respondent suggested to set a token fee. 	<ul style="list-style-type: none"> • Noted.
Unlicensed RAMCs	<ul style="list-style-type: none"> • Some participants of the consultative session requested the authorities to step up efforts against unlicensed RAMCs when the licensing regime is 	<ul style="list-style-type: none"> • The new legislation will require C&ED to take enforcement actions against unlicensed RAMC operations. C&ED will be

	in place.	empowered to arrest and detain persons operating unlicensed RAMCs and search business premises and seize documents and records therein.
Migration from Registration to Licensing of RAMCs	<ul style="list-style-type: none"> Some respondents suggested that there is no need for transitional arrangement. For those who considered a transition period necessary, a range of 1 to 3 years were suggested. 	<ul style="list-style-type: none"> We propose that existing RAMCs will have 60 days to apply for a licence upon the commencement of the relevant provisions, and they will be deemed licensed until their applications are approved/refused. (See item 40 of the detailed legislative proposals)
Appeal Mechanism	<ul style="list-style-type: none"> Most respondents agreed with the proposed establishment of an independent appeals tribunal, though a respondent considered that there is no need for a separate tribunal as the reviews can be conducted by the Securities and Futures Appeals Tribunal. Some respondents commented that members of the appeals tribunal should include representatives from the industry. 	<ul style="list-style-type: none"> To achieve general consistency in review of decisions made by the relevant authorities on AML breaches, we propose to establish an independent tribunal under the proposed legislation.
Assistance from Government and the Regulators	<ul style="list-style-type: none"> A number of respondents suggested that the regulatory authorities should set up enquiry hotlines as FIs may encounter difficulties in conducting CDD. 	<ul style="list-style-type: none"> The regulators will consider the relevant details in the implementation stage of the new legislation.
Training and publicity	<ul style="list-style-type: none"> FIs would like the regulators to provide appropriate training to facilitate their compliance with the future requirements. In this respect, 	<ul style="list-style-type: none"> Relevant authorities will consider providing appropriate training upon enactment of the proposed legislation.

	<p>some respondents considered that the current training efforts provided by financial regulators and the Police is adequate, while a respondent commented that training should be an ongoing process.</p> <ul style="list-style-type: none"> • A number of respondents suggested that the regulatory authorities and the Government should launch mass publicity on the new CDD requirements so that members of the public will be more cooperative in the CDD process. 	<ul style="list-style-type: none"> • Mass publicity will be arranged upon the enactment of the proposed legislation.
--	---	---