

**Joint meeting of the Panels on Administration of Justice
and Legal Services, Financial Affairs and Security**

Measures to Combat Terrorist Financing

Introduction

This paper addresses the issue of terrorist financing, the Hong Kong response, its existing legislation and the Financial Action Task Force's Special Recommendations and initiative. It does not address in detail the relevant United Nations Security Council Resolutions (UNSCR) or the International Convention for the Suppression of the Financing of Terrorism as these are dealt with in a separate paper entitled "Measures to combat terrorism".

Background

2. Following the attack on 11 September 2001 the US President George W Bush called for global efforts to starve terrorists of funding. This was echoed and supported by world leaders and countries throughout the world have responded with executive and legislative initiatives. Canada, Australia, Singapore and the UK have implemented the United Nations Security Council Resolution (UNSCR) 1373 which includes a wide range of anti-terrorist measures including those directed to attack terrorist financing. The UK has already put in place anti-terrorist legislation, while Canada has introduced an anti-terrorist bill, both of which include anti-terrorist financing provisions. Hong Kong has also pledged full support in the global fight against terrorism and terrorist financing. It has taken measures domestically and, in its leading role as President of the Financial Action Task Force (FATF), the foremost international anti-money laundering body, has been in the forefront of a global international initiative.

3. In terms of definition, terrorist financing has been variously described. The UNSCR 1373 refers to the "wilful provision or collection of funds ... with the intention that the funds should be used or in the knowledge that they are to be used, in order to carry out terrorist acts". "Terrorist financing" raises complex law enforcement issues. It is a financial offence which is not carried out for financial gain. It concerns the provision or collection of funds (from both legal and illegal sources) which are to be used for a criminal purpose. It is not restricted to funds which are derived from illegal sources.

The Hong Kong Response

4. Prior to 11 September 2001, Hong Kong had already enacted pursuant to the United Nations Sanctions Ordinance (Cap. 537), the United Nations Sanctions (Afghanistan) Regulation giving effect to the UNSCR 1267. The Regulation is aimed at combating terrorist financing by preventing the making of funds and other financial resources available to the Taliban.

5. On 12 October 2001, the United Nations Sanctions (Arms Embargo) (Afghanistan) Regulation commenced implementing UNSCR 1333 which requires all states to freeze funds and other assets of bin Laden, his associates and entities associated with him, including the Al Qaida organization, and to ensure that no funds or financial resources are made available for his benefit or that of his associates or entities. The Regulation implements the Resolution by prohibiting the payment of funds to, or making financial resources available to bin Laden or any person connected with him.

6. Following the designation by the UN Security Council Committee of persons and entities designated as individuals and entities of the Taliban, its undertakings or connected with bin Laden, the names of these persons and entities have now been gazetted and the relevant list circulated to financial institutions by the financial regulators in Hong Kong. The UNSCR 1267 and UNSCR 1333 have therefore been given full effect in Hong Kong.

7. The UNSCR 1373 passed on 28 September 2001 is wide ranging, dealing as it does with terrorist financing in the general sense. It calls upon all states to prevent and suppress the financing of terrorism, criminalize the wilful provision and collection of terrorist funds, freeze terrorist assets, prohibit the making of funds, economic resources, financial or related services for the benefit of terrorists or those owned or controlled by them and ratify and implement the International Convention for the Suppression of the Financing of Terrorism. Hong Kong is already taking steps as a matter of priority to implement the UNSCR 1373. Legislative proposals are under consideration and Hong Kong will report to the Central People's Government on progress as the PRC is required to submit a report to the UN Security Council Counter-terrorism Committee on or before 27 December 2001.

The Financial Regulators' Response

8. The Hong Kong Monetary Authority (HKMA), Securities and Futures Commission (SFC) and Insurance Authority (IA) already have in place guidelines for their respective financial institutions which set out detailed procedures to combat money laundering activities. Following the passage of the United Nations Sanctions (Afghanistan) Regulation and the United Nations Sanctions (Arms Embargo) (Afghanistan) Regulation, HKMA, SFC and IA

have issued advisory letters to the banking, securities and insurance industries to draw their attention to these Regulations and alert them to take the necessary steps to ensure compliance. They have also circulated lists of persons and entities gazetted under the Regulations with instructions that these should be checked against records and appropriate steps be taken. They continue to advise their respective institutions on updates of the lists.

9. On 24 September 2001 President Bush issued an Executive Order blocking property and prohibiting transactions with those who commit terrorism. In response, HKMA, SFC and IA notified their respective authorized institutions or regulatees to pay attention to the Executive Order, and to check whether they have had or currently have accounts, transactions or dealings with entities believed to be terrorists or terrorist organizations as designated in the Executive Order. The Police also issued a similar advisory to money changers and remittance agents. The regulators and the Police will continue to liaise with the relevant institutions and financial businesses to update them of the names designated by the US as terrorists. To date no such accounts suspected of or known to be connected with the designated names have been identified.

10. In addition to the above, the regulators have reminded those under their supervision of their obligation under Section 25A of the Organised and Serious Crimes Ordinance (Cap. 455) (OSCO) to watch out for any suspicious transactions relating to terrorists or their activities and to report them to the Joint Financial Intelligence Unit (JFIU) operated by the Police and Customs and Excise Department.

11. Overall, the financial institutions concerned have devoted more efforts to discern suspicious transactions against the designated names in association with the Regulations mentioned in paragraphs 4 and 5, and the Executive Order mentioned in paragraph 9. Compliance with these international and legal requirements is positive to Hong Kong's overall image both as an international financial centre and a place for business.

Law Enforcement Response

12. The Police have stepped up intelligence support for the United States since 11 September. The JFIU has been monitoring every suspicious transaction against the possibility of such transactions being connected to terrorists or terrorist type activity. All of the names mentioned in the US Executive Order have been checked and no connection with existing police records has been found. The JFIU has also received from the US a list of names allegedly related to bin Laden and has checked and notified the relevant US authorities that these names are not on Hong Kong's records. Steps have also been taken to check these names with the relevant financial institutions in Hong Kong. In addition, the JFIU has stepped up its investigation and

detection of large amount transactions relating to accounts in the Middle East. The JFIU will continue to provide its full support to its overseas counterparts and cooperate with them in tracing financial transactions suspected of being linked to terrorist activities.

The Hong Kong Regime

Criminalisation

13. At present, there is no anti-terrorism law of general application in Hong Kong but many offences typically committed by terrorists (e.g. murder, kidnapping, providing services that assist in the development of weapons of mass destruction, etc.) are offences under ordinary criminal laws. There is no offence of terrorist financing or offence of providing or collecting funds to be used to carry out terrorist acts. Legislative measures will be required to address this deficiency.

14. At present a person who provides funds to carry out any illegal activity may, in circumstances where there is specific knowledge as to the purpose of the funds and a causal connection between the provision of funds and the illegal activity, be charged with aiding and abetting the illegal activity. In addition, a person who deals in funds that he knows or has reasonable grounds to believe are proceeds of an indictable offence in Hong Kong or elsewhere is guilty of a money laundering offence under Section 25 of OSCO.

Freezing

15. It is essential that funds suspected of being connected to terrorism be frozen and thereafter confiscated and that there is machinery to enable this to be carried out as quickly and efficiently as possible. Procedures for freezing and confiscating funds are available under OSCO, the Drug Trafficking (Recovery of Proceeds) Ordinance (Cap. 405) (DTROP) and the Mutual Legal Assistance in Criminal Matters Ordinance (Cap. 525) (MLA).

16. The present OSCO and DTROP regimes allow for funds to be restrained and subsequently confiscated where a person has been charged with a specified offence and there is reason to believe he has benefited from that offence. Specified offences include money laundering and a number of terrorist type offences. The benefit must be derived or received in connection with the commission of the offence and confiscation will follow after conviction if the court is satisfied on a balance of probabilities that the person has so benefited. These regimes are conviction based and the confiscated funds must be derived from the offence. Such regimes have worked well in the context of serious crime and drug trafficking where crime is normally carried out for a financial motive. Terrorist financing will however calls for a different regime

as the property to be frozen or confiscated is not proceeds of or derived from an offence. It may instead be legitimately sourced and intended either to finance a terrorist act, a terrorist or his organization. In addition, there may be no conviction to underpin the order.

17. Hong Kong can also provide international legal assistance under its MLA regime by registering as an external confiscation order a court order from an overseas jurisdiction in respect of a serious external offence, i.e. an offence with a penalty of two years or more imprisonment on conviction. The order, once registered, may be enforced against property in Hong Kong. A restraint order can be obtained prohibiting dealing in any property in Hong Kong pending registration and enforcement of the external confiscation order. Such mutual legal assistance requests have been utilized successfully on previous occasions between the United States, Australian and Hong Kong authorities. However, the MLA procedures can only be utilized where the overseas criminal act constitutes a criminal offence in Hong Kong, and are therefore not available at present for offences of terrorist financing unless some general criminal offence is made out under Hong Kong law. This can however be rectified in the legislative proposals to implement UNSCR 1373 amongst others.

18. The United Nations Sanctions (Afghanistan) Regulation and the United Nations Sanctions (Arms Embargo) (Afghanistan) Regulation, albeit they do not contain a specific freezing power, effectively prevent the payment of funds to the Taliban and bin Laden and other gazetted entities without the need for either conviction or an inquiry into the legitimacy of the funds.

19. The International Convention for the Suppression of the Financing of Terrorism and the FATF Special Recommendations require jurisdictions not only to freeze terrorist funds but also to confiscate them. Hong Kong cannot at present comply with this requirement. It is necessary to address this issue through legislative amendments including the addition of terrorist financing as a specified offence under OSCO, and possibly removal of the need for conviction and a nexus between the offence and the funds.

Suspicious Transaction Reporting

20. Reporting suspicious transactions is the first step in identifying and freezing funds. It has also proved to be an invaluable tool in tracing the movements of terrorists and identifying their associates and financial backers.

21. In Hong Kong any person legal or natural who knows or suspects any property is the proceeds of or used in or intended to be used in connection with an indictable offence is required to disclose that suspicion to an authorized officer. The indictable offence needs not be committed in Hong Kong. This obligation extends to lawyers and accountants who are not excused by reason of

professional privilege. Reports are made to the JFIU. Since 11 September 2001 the Police and financial regulators have reminded the relevant institutions and businesses within their remits of this obligation.

The Financial Action Task Force

22. Hong Kong is currently presiding over the Financial Action Task Force (FATF). An extraordinary FATF Plenary meeting under Hong Kong's Presidency was held in Washington DC on 29-30 October 2001. At that meeting the FATF expanded its mission beyond money laundering to cover terrorist financing. During the same meeting the FATF also agreed to eight wide ranging Special Recommendations which commit members to:

- take immediate steps to ratify and implement the relevant United Nations instruments, including the International Convention on the Suppression of the Financing of Terrorism;
- criminalize the financing of terrorism, terrorist acts and terrorist organizations;
- freeze and confiscate terrorist assets;
- report suspicious transactions linked to terrorism;
- provide the widest possible range of assistance to other countries' law enforcement and regulatory authorities for terrorist financing investigations;
- impose anti-money laundering requirements on alternative remittance systems;
- strengthen customer identification measures in international and domestic wire transfers; and
- ensure that entities, in particular non-profit organizations, cannot be misused to finance terrorism.

23. A copy of the Special Recommendations is Annexed. In order to ensure swift and effective implementation of these new standards it was agreed that a self-assessment against the Recommendations by all members is to be completed by 31 December 2001 with compliance expected by June 2002. All jurisdictions will be invited to engage in the self-assessment exercise through an outreach process involving the FATF style regional bodies. In June 2002 FATF will consider identifying those jurisdictions that have inadequate measures to fight terrorism-financing, failure to comply with the Special Recommendations being the benchmark.

The Hong Kong Response to FATF's Special Recommendations

24. Hong Kong as President of FATF has been in a position to steer the global response to terrorist financing. It is imperative that Hong Kong should be in compliance with the new standards adopted. The following issues are relevant.

25. In respect of Recommendation I Hong Kong has already implemented UNSCRs 1276 and 1333. Legislative proposals to implement UNSCR 1373 is presently under consideration. The PRC signed the International Convention for the Suppression of the Financing of Terrorism on 13 November 2001. Hong Kong will discuss with the PRC on the implementation of the Convention in Hong Kong.

26. Recommendation II requires all members to criminalize terrorist financing and ensure that it is designated as a money-laundering predicate offence. Although the existing Hong Kong regime does not effectively implement this Recommendation, the introduction of an appropriate offence provision in the legislative proposals to implement UNSCR 1373 amongst others will ensure compliance.

27. At present, Hong Kong is not in compliance with Recommendation III. The introduction of a restraint power in the legislative proposals to be introduced pursuant to UNSCR 1373 amongst others will implement the Recommendation in so far as it relates to freezing. Options as to how to implement the Recommendation in so far as it relates to confiscation need to be considered.

28. Recommendation IV extends the suspicious transaction regime to terrorist acts, terrorism and terrorist organizations. Hong Kong is considered to be in compliance as the existing regime requires reporting of funds connected to an indictable offence. Most terrorist type offences in Hong Kong can be categorized as indictable offences. Legislative proposals currently under consideration categorize terrorist financing as an indictable offence.

29. Recommendation V refers to mutual cooperation and information sharing. Hong Kong is already in a position to afford international cooperation in criminal matters through the MLA regime and the Fugitive Offenders Ordinance (Cap. 503). The Recommendation however extends the requirement to proceedings and investigations relating to the financing of terrorism, terrorist acts and terrorist organizations. As this is not yet an offence, Hong Kong will be in partial compliance with this Recommendation unless the underlying acts make out some other general criminal offence under Hong Kong law.

30. Recommendation VI addresses the problem of alternative remittance systems. Although Hong Kong now requires all money changers and remittance changers to be registered with the Police and to comply with know your customer and record keeping requirements, they are unregulated and not subject to all the FATF Recommendations that apply to banks and non-banking financial institutions. The present regime does not meet standards of comparable jurisdictions and Hong Kong will need to consider ways to address this.

31. Hong Kong is generally in compliance with Recommendation VII in that authorised institutions under the Banking Ordinance are already encouraged, to the maximum extent possible, to provide customer identification in wire transfers.

32. Recommendation VIII addresses concerns that some non-profit making organizations have been used or may be vulnerable to abuse as vehicles for the collection and dissemination of terrorist funds or to terrorist organizations. Hong Kong will address this issue initially by reviewing the manner in which some non-profit organizations such as charities are regulated.

Next Step

33. The Administration is according high priority to implementing UNSCR 1373, and is taking necessary steps to implement the FATF's Special Recommendations. It will also liaise with China on implementation of the International Convention for the Suppression of the Financing of Terrorism. Meanwhile, the Administration is also keeping the development of the global initiative on terrorist financing in view, and will continue to work with the financial regulators and law enforcement agencies closely on this subject.

Security Bureau and Financial Services Bureau
November 2001