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**Panel on Financial Affairs**

**Special meeting on 24 May 2010**

**Background brief on the proposed new anti-money laundering legislation  
for financial institutions**

**Purpose**

This paper provides background information on the proposed new anti-money laundering legislation (AML)<sup>1</sup> for financial institutions, and a summary of Members' views and concerns on the subject during relevant discussions at meetings of the Panel on Financial Affairs (the Panel).

**Background**

Mutual evaluation conducted by the Financial Action Task Force

2. The Financial Action Task Force (FATF) is an inter-governmental body which sets international AML standards generally known as the FATF Recommendations. Members of FATF, including Hong Kong, are obliged to implement the FATF Recommendations. FATF has been conducting mutual evaluation (ME) on its member jurisdictions against the FATF Recommendations with a view to ascertaining the effectiveness of the AML systems of these jurisdictions and putting forward proposals on improvement measures.

3. The ME on Hong Kong was conducted in November 2007 and the ME Report was published in July 2008. In the Report, FATF recognized the strengths of Hong

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<sup>1</sup> For the purpose of the legislative proposal, anti-money laundering includes the meaning of both anti-money laundering and counter financing of terrorism.

Kong's AML regime, but also highlighted inter alia that the lack of statutory backing and appropriate sanctions for customer due diligence (CDD) and record keeping requirements for financial institutions and the absence of an AML regulatory regime for remittance agents and money changers (RAMCs) are major deficiencies that should be addressed.

4. Hong Kong is required to report to FATF on actions taken or planned to address the deficiencies identified in the ME on a regular basis, and the first progress report is due in the second quarter of 2010. According to FATF's procedure, jurisdictions required to submit post-ME follow-up reports to FATF are expected to have made substantial progress in their first report, and they are expected to seek removal from the follow-up process about three years after the ME, which means 2011 in the case of Hong Kong.

#### Existing AML regulatory regime

5. At present, the basic requirements on CDD and record-keeping by financial institutions are implemented through guidelines issued by the financial regulators, viz. the Hong Kong Monetary Authority, the Securities and Futures Commission and the Insurance Authority pursuant to their respective statutory powers under the Banking Ordinance (Cap. 155), the Securities and Futures Ordinance (Cap. 571) and the Insurance Companies Ordinance (Cap.41). Currently there is no specific provision for sanctions against non-compliance with these guidelines, but such non-compliance will be taken into account in the financial regulators' consideration of the "fitness and properness" of the regulatees.

6. RAMCs are currently subject to the statutory requirements under sections 24B and 24C of the Organized and Serious Crimes Ordinance (OSCO) (Cap. 455) to be registered with the Joint Financial Intelligence Unit of the Police, to verify customers' identity for transactions or wire transfers of HK\$8,000 or above and to keep records of such transactions for a specified period. There is however no statutory provision for the power to refuse registration and the power to access RAMC's premises or books/records for compliance checks. FATF has recommended enhancement of the AML regulation over this sector.

#### **Broad framework of the proposed legislation**

7. On 11 June 2009, the Administration briefed the Panel on the broad framework of the proposed legislation which sought to -

- (a) provide statutory backing for CDD and record-keeping requirements on financial institutions;

- (b) confer supervisory and enforcement powers on the regulatory authorities in respect of the compliance of financial institutions with the statutory CDD and record-keeping requirements;
- (c) provide for criminal sanctions and supervisory sanctions for non-compliance; and
- (d) put in place an AML regulatory regime for RAMCs, under which RAMCs will be required to obtain a licence from the Customs and Excise Department (C&ED).

8. During the Panel discussion, members generally supported the policy objective and direction of the proposed legislative framework for the AML regulatory regime. Individual members expressed the following concerns:

- (a) given the relatively small scale of business operation of RAMCs, the proposed licensing requirements for RAMC might create excessive burden on RAMCs and reduce their room for survival. The Administration should consider allowing a transitional period for RAMCs in implementing the various new regulatory measures;
- (b) the Administration should provide in the legislation necessary checks and balances on the enforcement powers of the regulatory authorities and a clearly defined mental threshold for the criminal liabilities that may be incurred by financial institutions for non-compliance;
- (c) apart from criminal sanctions, the Administration should consider different regulatory sanctions such as fines or suspension of licence for non-compliance of financial institutions. Reference should be made to the international best practice in this regard; and
- (d) the Administration should impose on the financial institutions the minimum necessary AML regulatory requirements to achieve a proper balance between regulatory oversight and compliance burden on the institutions concerned.

9. On 9 July 2009, the Administration launched a three-month public consultation on the conceptual framework of the proposed new legislation. According to the Administration, a total of 39 written comments were received during the consultation, and more than 800 participants had attended the seven sector-specific consultation sessions organized by the Administration in conjunction with the regulatory authorities. The majority of respondents acknowledged the importance for Hong Kong to comply with the international AML standards, and there was broad support for the Government's proposal to introduce new legislation to enhance the AML regulation of financial institutions and to introduce a licensing system to regulate RAMCs.

## **Detailed proposals on the AML regulatory regime**

10. Taking into account the comments received in the consultation exercise, the Administration drew up a set of detailed legislative proposals in consultation with the regulators and issued a consultation document on 7 December 2009 to conduct a further round of public consultation. The consultation ended on 6 February 2010.

11. On 14 December 2009, the Administration briefed the Panel on the detailed legislative proposals which included the following key elements -

- (a) the proposed legislation will stipulate the detailed CDD and record-keeping obligations to be met by financial institutions;
- (b) the threshold that triggers CDD requirements for money changing transactions be raised from \$8,000 at present as provided under the OSCO to \$120,000;
- (c) the existing threshold of \$8,000 for obtaining and verifying customers' information for remittance transactions as provided under OSCO will be maintained;
- (d) financial institutions will be permitted to continue to rely on local third parties (i.e. lawyers, accountants, and trust and company service providers) for conducting CDD on customers for a period of, say, three years;
- (e) the proposed legislation will provide for both criminal as well as supervisory sanctions subject to safeguards in the legislation;
- (f) the proposed legislation will introduce a single category of personal criminal liability with a clearly-defined mental threshold, such that only those who contravene the statutory obligations with knowledge or intent to defraud commit an offence and shall be liable to criminal fines and/or imprisonment upon summary conviction or indictment;
- (g) an independent tribunal will be established to review decisions made by the relevant authorities, including the imposition of supervisory sanctions and licensing of RAMCs;
- (h) the proposed legislation will commence one year after the enactment of the legislation; and

- (i) the proposed legislation will provide for a 60-day transitional period upon the implementation of the licensing regime for registered RAMCs to apply for a RAMC licence.

12. During the Panel discussion, members expressed support for the legislative proposals in principle. Pointing out that under the current regime where a number of banks had refused to provide account services to RAMCs, a member considered that the proposed licensing system for RAMCs would help improve the operational environment of RAMCs by alleviating the concerns of the banking sector about possible money-laundering activities involved in the remittance and money changing business of RAMCs. Another member commended the Administration for taking on board the views of the financial sectors by raising the threshold for CDD requirements for money changing transactions from \$8,000 to \$120,000 and introducing a single category of personal criminal liability with a clearly-defined mental threshold. Members urged the Administration to actively engage the stakeholders in its consultation on the detailed legislative proposals.

### **Recent developments**

13. According to the information provided by the Administration to the Panel in late March 2010, during the public consultation on the detailed legislative proposals, the Administration had organized eight sector-specific consultative sessions, which were well attended with over 800 participants. In addition, the Administration had received 45 written comments from individuals, financial institutions, professional bodies and trade associations. The Administration planned to publish the consultation conclusion report when it introduced the relevant Bill into the Legislative Council, which was scheduled for the second quarter of 2010.

14. The Panel will hold a special meeting on 24 May 2010 to hear the views of relevant parties and members of the public on the detailed legislative proposals.

### **References**

- 15. The relevant papers are available at the following links:

Administration's paper for the Panel meeting on 11 June 2009

<http://www.legco.gov.hk/yr08-09/english/panels/fa/papers/fa0611cb1-1829-2-e.pdf>

Minutes of Panel meeting on 11 June 2009 (paragraphs 15 to 26)

<http://www.legco.gov.hk/yr08-09/english/panels/fa/minutes/fa20090611.pdf>

Administration's consultation paper on the conceptual framework of the legislative proposal

<http://www.legco.gov.hk/yr08-09/english/panels/fa/papers/facb1-2247-e.pdf>

Administration's consultation paper on the detailed legislative proposal  
<http://www.legco.gov.hk/yr09-10/english/panels/fa/papers/fa1214cb1-587-1-e.pdf>

Administration's paper for the Panel special meeting on 14 December 2009  
<http://www.legco.gov.hk/yr09-10/english/panels/fa/papers/fa1214cb1-601-11-e.pdf>

Minutes of Panel special meeting on 14 December 2009 (paragraphs 32 to 35)  
<http://www.legco.gov.hk/yr09-10/english/panels/fa/minutes/fa20091214.pdf>

Letter from the Administration dated 24 March 2010  
<http://www.legco.gov.hk/yr09-10/english/panels/fa/papers/facb1-1465-1-e.pdf>

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