

LEGISLATIVE COUNCIL PANEL ON FINANCIAL AFFAIRS

Proposed New Anti-Money Laundering Legislation for Financial Institutions – Detailed Legislative Proposals

Purpose

This paper sets out the detailed legislative proposals on the customer due diligence (CDD) and record-keeping requirements for financial institutions and the regulation of remittance agents and money changers (RAMCs); and reports the comments received in the consultation on the conceptual framework of the legislative proposals which was completed in October 2009.

Background

2. We briefed the Legislative Council Financial Affairs Panel on 11 June 2009 on the conceptual framework of the legislative proposals. As explained in the Panel paper no. CB(1)1829/08-09(02), the lack of statutory backing and appropriate sanctions for CDD and record-keeping requirements and the absence of an anti-money laundering (AML) regulatory regime for RAMCs in Hong Kong were considered by the Financial Action Task Force (FATF) as major deficiencies in our AML regime that should be addressed. Hong Kong is required to take follow-up actions to substantially improve our AML regime by 2011. The proposed legislation seeks to address the above deficiencies.

3. At the meeting in June 2009, Members indicated general support to the Government's objective of the proposed legislative exercise and noted that we would conduct consultation to gauge views from the financial sectors and the public on the conceptual framework of the legislative proposals. The consultation exercise commenced on 9 July 2009 and ended on 8 October 2009.

Comments Received in the Last Round of Consultation

4. We received a total of 39 written comments. During the consultation period, the Financial Services and the Treasury Bureau, in conjunction with the Hong Kong Monetary Authority (HKMA), the Securities and Futures Commission (SFC), the Insurance Authority (IA), the Police and the Customs and Excise Department (C&ED) organized seven sectoral consultation sessions to listen to views from industry practitioners on the broad framework. Members of the public were welcomed to attend these sessions. These sessions were attended by a total of more than 800 participants.

5. In gist, the majority of respondents acknowledged the importance for Hong Kong to comply with the international AML standards in order to maintain our status as an international financial centre, and there is 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.

6. Taking into account the comments expressed in the consultation exercise, we have drawn up a set of detailed legislative proposals in consultation with the regulators. The objective is to codify in statute the international AML standards in respect of CDD and record-keeping. We have issued a consultation document on 7 December 2009 to conduct a further round of consultation¹. The detailed proposals are set out in Annex A to the consultation document and the major comments received in the last round of consultation with the Administration's response are set out in Annex B to the consultation document.

Detailed Legislative Proposals

7. The detailed legislative proposals consist of the following key elements:

¹ Hard copies of the consultation document have been delivered to the Legislative Council Secretariat on 7 December 2009. The consultation document is available at the following website: www.fstb.gov.hk/fsb/aml/eng/consultation/consultation.htm

Coverage (Items 1 and 2 of Annex A to the consultation document)

- (a) Authorized institutions, licensed corporations, insurers, insurance agents and brokers and RAMCs will be subject to the requirements under the new legislation. In line with the institution-based approach adopted in the existing financial regulatory regime, HKMA, SFC, IA and C&ED will be designated as the relevant authorities for supervising AML compliance by the banking, securities, insurance and RAMC sectors respectively.

Obligations (Items 3 to 19 of Annex A to the consultation document)

- (b) The proposed legislation will stipulate the detailed CDD and record-keeping obligations to be met by financial institutions (FIs), including the circumstances under which CDD should be conducted, the extent of CDD measures applicable to customers of different risk profiles, the classification of customers of different risk profiles, the specific requirements on wire transfers and remittance transactions, the requirements for ongoing due diligence, the actions required when unable to complete CDD, the types of records required to be maintained and the period for record retention, and officers' duty in ensuring proper systems to prevent non-compliance.
- (c) In view of the relatively low money laundering risks involved in money changing transactions and having regard to the maximum threshold permitted by FATF of US/EURO\$15,000, we propose that the threshold that triggers CDD requirements for money changing transactions be raised from \$8,000 at present as provided under the Organized and Serious Crimes Ordinance, Cap. 455 (OSCO) to \$120,000. Since money changing is a major business activity conducted by RAMCs, the proposed relaxation of the threshold would help alleviate the concerns of the RAMC sector over the proposed AML regulation and would also ensure that the new AML regime would not impact on the tourism industry.
- (d) We propose to maintain the existing threshold of \$8,000 for obtaining and verifying customers' information for remittance transactions as provided under OSCO. This level is already the maximum threshold permitted by

FATF (US/EURO\$1,000) for remittance transactions which is generally considered to involve higher money laundering risks.

- (e) We propose to permit FIs to continue to rely on local third parties (i.e. lawyers, accountants, and trust and company service providers) for conducting CDD on customers in introduction of business under the existing arrangement allowed for in the guidelines issued by the financial regulators if the latter can demonstrate to the FIs that they have adequate procedures to prevent money laundering, for a period of, say, 3 years. This will allow time for these sectors to be regulated as required by FATF if reliance on third parties is to be permitted. Currently the Security Bureau is working on this in consultation with the relevant sectors.

Powers of the Relevant Authorities (Items 20 to 31 of Annex A to the consultation document)

- (f) As set out in the conceptual framework, the proposed legislation will provide that the relevant authorities may access the business premises of FIs and their books and records, require information and answers from FIs and other persons, initiate investigations into suspected breaches, apply to the Magistrate for warrants for search and seizure, initiate summary prosecutions, and share information with overseas regulators. The exercise of the powers of the relevant authorities will be subject to appropriate procedural safeguards, e.g. inspections can only be carried out at a reasonable time during ordinary business hours, an inspector or investigator must provide evidence of authorization, search and seizure can only be done upon court warrants, self-incriminating evidence shall not be used against a person in a criminal proceedings, etc.
- (g) The proposed legislation will empower the relevant authorities to issue guidelines to facilitate AML compliance. Such guidelines will be non-statutory in nature but will have evidential value in determining whether the statutory obligations have been breached. We propose that HKMA, SFC, IA & C&ED should produce a generic set of guidelines which will be applicable to all relevant financial sectors so as to enhance consistency in compliance requirements and enforcement standards.

Under this generic set of guidelines, individual regulators will draw up their own sectoral guidelines to cover measures relevant to transactions specific to their respective regulated sectors.

Sanctions (Items 32 to 37 of Annex A to the consultation document)

- (h) With reference to the example of many jurisdictions, including the UK, the US, Singapore, Italy and Norway which have provided for criminal offences under their AML legislation in dealing with breaches of CDD and record-keeping requirements, we propose to provide for both criminal as well as supervisory sanctions subject to safeguards in the new legislation.
- (i) Taking into account the comments received in the consultation exercise that there should be a high mental threshold if the new legislation should provide for criminal liability on individuals, we propose to 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.
- (j) The relevant authorities will be empowered to impose supervisory sanctions where appropriate, including issuing directions for remedial action, public reprimands, and supervisory fines.

Licensing Regime for RAMCs (Items 38 to 53 of Annex A to the consultation document)

- (k) The proposed legislation will stipulate that any person who conducts money changing and remittance services “as a business” is required to obtain a licence from C&ED. This definition² will exempt business entities providing remittance or money changing services incidental to transactions related to their main business (e.g. retail businesses accepting

² With regard to FATF’s requirement that any entities providing remittance services should be subject to AML regulation by a competent authority, since the Post Office currently offers remittance services to the general public through a commercial remittance network system, the proposed legislation will cover the Post Office.

Renminbi in transactions) from the requirement to obtain licences.

- (l) The proposed legislation will provide for the details of the licensing regime for RAMCs to be administered by C&ED, including the functions and powers of C&ED as the licensing authority, coverage of the licensing regime, “fit and proper” criteria for RAMC licensees, and the offence for unlicensed RAMC operations.
- (m) To facilitate a smooth migration and having regard to views of the RAMC sector received in the consultation exercise, we propose that the new legislation should provide for a 60-day transitional period upon the implementation of the licensing regime for registered RAMCs to apply for a RAMC licence.

Appeals Mechanism (Items 54 to 60 of Annex A to the consultation document)

- (n) To ensure that there are proper checks and balances, we propose to establish an independent tribunal to review decisions made by the relevant authorities under the new legislation, including the imposition of supervisory sanctions and licensing of RAMCs. The proposed tribunal will comprise a Chairman (with qualifications for appointment as a judge of the High Court) and not less than two members to be appointed by SFST on a term of appointment not exceeding three years. The Chairman and members of the tribunal shall not be public officers.

Next Steps

8. We will proactively engage the relevant industry practitioners to gauge their views on the detailed legislative proposals during the further round of consultation. As in the last round of consultation, we have sent copies of the consultation document to trade associations, professional bodies and members of the relevant sectors and invited their views on the detailed legislative proposals. The consultation period will end on 6 February 2010. We will, in conjunction with the relevant regulators, arrange consultative sessions with members of individual financial sectors during the consultation period.

9. We will prepare draft legislation taking into account the views of Members and comments received from this round of consultation. Subject to progress made for the preparatory work, we aim to introduce the bill into the Legislative Council in Q2, 2010.

**Financial Services and the Treasury Bureau
December 2009**