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Panel on Financial Affairs

Meeting on 6 January 2014

**Background brief on retention of a supernumerary directorate post in the
Office of the Commissioner of Insurance for enforcing the anti-money
laundering regime and regulating relevant
mandatory provident fund intermediaries**

Purpose

This paper provides background information on the staffing proposal of retaining a supernumerary post of Assistant Commissioner of Insurance ("ACI") (D2) for enforcing the anti-money laundering ("AML") regime and regulating relevant mandatory provident fund ("MPF") intermediaries. It also summarizes the major concerns and views expressed by Members during discussions on the staffing proposal and other related issues in 2011 and 2012.

Background

Anti-money laundering regime and the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance

2. The Financial Action Task Force ("FATF") is an inter-governmental body and its recommendations are regarded as the prevailing international AML and counter-terrorist financing standards. Hong Kong joined FATF in 1990 and is obliged to implement FATF's requirements as well as subject to its process of Mutual Evaluation in monitoring progress made by jurisdictions in implementing FATF's requirements.

3. FATF conducted a Mutual Evaluation on Hong Kong in 2007-2008 to assess the compliance of Hong Kong's AML regime with FATF's Recommendations. Having regard to FATF's recommendations made in the Mutual Evaluation¹, the Administration considered that new legislation should be put in place to enhance the AML regulatory regime of the financial sectors.

4. The Administration introduced the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Bill ("AML Bill") into the Legislative Council ("LegCo") on 10 November 2010. A Bills Committee was formed to scrutinize the AML Bill, which was enacted as the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance ("AMLO") on 29 June 2011. AMLO commenced operation on 1 April 2012.

5. AMLO stipulates the customer due diligence ("CDD") measures and record-keeping requirements to be undertaken by financial institutions in line with the international AML standards as promulgated by FATF. The Insurance Authority ("IA") is the relevant authority under AMLO to supervise compliance by insurers and insurance intermediaries viz. insurance brokers and insurance agents (collectively referred to as "insurance institutions" hereunder) with the statutory CDD and record-keeping obligations. Under AMLO, IA is empowered to conduct routine inspections on insurance institutions, investigate suspected breaches, impose disciplinary sanctions and initiate prosecution against criminal offences committed by insurance institutions. IA is also empowered to issue guidelines on the details in respect of the statutory CDD and record-keeping obligations to facilitate compliance by insurance institutions.

Mandatory Provident Fund Schemes (Amendment) Ordinance 2012 and the Employee Choice Arrangement

6. The Mandatory Provident Fund Schemes Ordinance (Cap. 485) ("MPFSO") was enacted in 1995 to provide a statutory framework for the establishment of mandatory, privately managed retirement schemes for the retirement protection of the general workforce. The Mandatory Provident Fund ("MPF") System was launched in December 2000 after passage of relevant subsidiary legislation in 1998, 1999 and 2000. The Mandatory Provident Fund Schemes Authority ("MPFA") regulates MPF intermediaries through its Code of Conduct and is responsible for setting standards and registration of MPF intermediaries. Supervision of registered MPF intermediaries rests with the frontline regulators ("FRs"), i.e. the Hong Kong

¹ The 2007-2008 Mutual Evaluation on Hong Kong identified a number of issues in Hong Kong's AML regime, including the lack of a statutory backing for customer due diligence and record-keeping requirements as well as the lack of appropriate sanctions for breach of such requirements.

Monetary Authority ("HKMA"), IA and Securities and Futures Commission ("SFC") under their respective ordinances.

7. In July 2009, the Mandatory Provident Fund Schemes (Amendment) Ordinance 2009 was enacted to amend MPFSO to provide the statutory basis to introduce the Employee Choice Arrangement ("ECA")². With rising public expectation towards investor protection and in anticipation of more proactive sales and marketing activities targeted at MPF scheme members upon implementation of ECA, the Administration considered it prudent to put in place a statutory framework for the regulation of registered MPF intermediaries to facilitate implementation of ECA for the better protection of MPF scheme members.

8. On 14 December 2011, the Administration introduced into LegCo the Mandatory Provident Fund Schemes (Amendment) (No. 2) Bill 2011 (" the MPF Bill"), which sought to amend MPFSO to provide for a statutory regulatory regime for MPF intermediaries to facilitate implementation of ECA and for related matters. A Bills Committee was formed to study the MPF Bill which was enacted as the Mandatory Provident Fund Schemes (Amendment) Ordinance 2012 ("MPFO 2012") by LegCo on 21 June 2012. MPFO 2012 and ECA both came into operation on 1 November 2012.

9. Under MPFO 2012, IA is given the statutory role as the FR responsible for the supervision and investigation of registered MPF intermediaries whose main line of business is in the insurance sector. IA would help ensure compliance by MPF intermediaries from the insurance sector with the conduct and other relevant statutory requirements specified in MPFO 2012 and the Code of Conduct to be issued by MPFA. In performing these regulatory functions, IA would maintain close liaison with MPFA and the other frontline regulators in the regulatory process, and assume new enforcement duties under the MPFO 2012.

Creation of a supernumerary post of ACI

10. For the purpose of performing new regulatory functions stipulated in the AMLO and MPFO 2012, the Administration proposed to create a supernumerary post of ACI in OCI of the Financial Services Branch under FSTB for a period of 24 months and briefed the Panel on Financial Affairs ("FA Panel") on the staffing proposal at the meeting on 6 February 2012. The

² ECA will allow MPF scheme members to transfer accrued benefits derived from their own mandatory contributions during current employment from a contribution account under an MPF scheme on a lump-sum basis to another MPF scheme of their own choice at least once per calendar year.

staffing proposal was endorsed by the Establishment Subcommittee ("ESC") at the meeting on 2 May 2012 and subsequently approved by the Finance Committee ("FC") at the meeting on 25 May 2012. The main responsibilities of the ACI post are –

- (a) To oversee the implementation of AML regulatory regime for the insurance sector upon the commencement of AMLO, including mapping out the detailed implementation plans on inspection, investigation of non-compliance cases, disciplinary process and prosecution of insurance institutions.
- (b) To liaise with the insurance industry on the latter's compliance with the new statutory AML requirements and review the industry guidelines issued under the AMLO to promote and facilitate compliance by insurance institutions.
- (c) To set up the system for supervision of MPF intermediaries from the insurance sector, including compliance monitoring, inspection, investigation, complaints handling and promulgation of implementation details, and to oversee the implementation of the new regulatory system upon commencement of the legislation on the regulation of MPF intermediaries.
- (d) To represent IA in the close liaison with the other AML and MPF intermediaries regulators.
- (e) To liaise with the existing insurance intermediaries self-regulatory bodies and other financial regulators on the transitional arrangements with a view to taking over the MPF intermediaries supervision.
- (f) To design educational programmes for MPF intermediaries from the insurance sector on the new regulatory procedures.

Deliberations at the meeting of the Panel on Financial Affairs and the Establishment Subcommittee

11. When the staffing proposal was discussed at the meeting of FA Panel on 6 February 2012, members expressed concern about the need to have adequate staff to undertake the work of OCI during the transition period before the independent Insurance Authority ("IIA") was formally established and enquired

about the arrangement for OCI staff who were on supernumerary and/or contract terms when IIA was established.

12. The Administration responded that OCI would continue to perform all its functions until the establishment of the new IIA, including the additional work arising from new legislation relating to the regulation of MPF intermediaries and the enhancement of AML regulatory regime. The Administration was discussing internally the arrangement for the existing OCI staff.

13. When the staffing proposal was discussed at the meeting of ESC on 2 May 2012, Members agreed that there was a pressing need to create the post having regard to OCI's new duties of supervising registered MPF intermediaries and strengthening the anti-money laundering regulatory regime of the insurance sector.

Deliberations of the Bills Committee on the Mandatory Provident Fund Schemes (Amendment) (No. 2) Bill 2011

14. The relevant views and concerns raised by members the Bills Committee are summarized in the ensuing paragraphs.

Regulatory approach

15. The Bills Committee noted that under the proposed regulatory regime for MPF intermediaries, MPFA would be the authority to administer the registration of MPF intermediaries, issue guidelines on compliance with statutory requirements applicable to registered MPF intermediaries, and impose disciplinary sanctions, while HKMA, IA and SFC would be given the statutory role as FRs responsible for the supervision and investigation of registered MPF intermediaries whose core business was in banking, insurance and securities respectively. Some members expressed concern that the proposed regulatory approach, which involved MPFA and the three FRs, might give rise to inconsistencies in supervision and enforcement standards, and enquired about the delineation of responsibilities between MPFA and the three FRs, as well as measures for ensuring regulatory consistency and a level playing field.

16. The Administration advised that the proposed regulatory approach would ensure consistency and efficient use of regulatory resources as MPF intermediary activities were incidental to the main lines of business of most MPF intermediaries, who were subject to the supervision of the respective FRs for their main lines of business. The Administration also highlighted measures

to ensure regulatory consistency and a level playing field, including MPFA is required to consult the FRs in making rules on conduct requirements and issuing guidelines on compliance with the proposed statutory requirements; MPFA and the FRs would sign Memorandum of Understanding setting out their respective powers and functions and the detailed arrangements in supervision of MPF intermediaries; and MPFA would establish a regular liaison mechanism with the FRs to enhance communication among them, etc.

Supervision and investigation arrangements

17. The Bills Committee sought details on the supervisory and investigation arrangements for the proposed regulatory regime, including the regulatory tools to be adopted by the FRs to ascertain compliance and the coordination among MPFA and the FRs in this regard.

18. The Administration advised that FRs would formulate their supervision strategies and plans taking into account the actual MPF market operations and activities under the new regime, drawing expertise and experience from intermediary regulation in their own respective sectors, as well as through liaison with MPFA and the FRs. MPFA had established a regular liaison forum with the FRs to enhance inter-regulator communication.

Handling of complaints

19. The Bills Committee was concerned that as the proposed regulatory regime involved MPFA and the three FRs, members of the public might need to approach and deal with different regulators in lodging complaints against MPF intermediaries. In response, the Administration and MPFA advised that a "one-stop" approach would be adopted for handling of complaints. Under the approach, MPFA would receive all complaints against intermediaries and be responsible for the initial processing to maintain an oversight of all complaints. MPFA would then refer the complaints to the relevant FRs for follow-up. Furthermore, MPFA would receive regular updates from RFs on the progress of their investigations so that it could inform the complainant of the outcome.

Council Questions

20. Since enactment of MPFO 2012, Members raised three questions at the LegCo meetings of 24 October 2012, 5 December 2012 and 6 November 2013 on ECA. Major issues covered in these questions included: whether the Administration would review the efficacy of ECA, impacts of ECA on fees of MPF schemes, information dissemination of MPF schemes and regulation on

malpractices in MPF sales. Details of the questions and the Administration's replies are given in the **Appendix I**.

Latest development

21. The supernumerary ACI post created in FSB of FSTB will lapse in May 2014. The Administration will brief FA Panel at the coming meeting on 6 January 2014 on the proposal to retain the post for enforcing AML regime and regulating relevant MPF intermediaries.

Relevant papers

22. A list of relevant papers is given in the **Appendix I**.

Council Business Division 1
Legislative Council Secretariat
2 January 2014

List of relevant papers

Date	Event	Paper/Minutes of meeting
29 June 2011	The Legislative Council passed the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Bill	Hansard Bill passed Report of the Bills Committee (LC Paper No. CB(1)2586/10-11)
6 February 2012	The Panel on Financial Affairs ("FA Panel") was briefed on the staffing proposal to create the supernumerary post of Assistant Commissioner of Insurance in the Office of the Commissioner of Insurance of the Financial Services Branch of the Financial Services and the Treasury Bureau for enforcing the anti-money laundering regime and regulating relevant Mandatory Provident Fund intermediaries	Administration's paper (LC Paper No. CB(1)959/11-12(04)) Minutes (LC Paper No. CB(1)1417/11-12)
2 May 2012	Meeting of the Establishment Subcommittee	Administration's paper (LC Paper No. EC(2012-13)3) Minutes (LC Paper No. ESC40/11-12)
25 May 2012	Meeting of the Finance Committee	Minutes (LC Paper No. FC181/11-12)

Date	Event	Paper/Minutes of meeting
21 June 2012	The Legislative Council passed the Mandatory Provident Fund Schemes (Amendment) (No. 2) Bill 2011	Hansard Bill passed Report of the Bills Committee (LC Paper No. CB(1)2068/11-12)
24 October 2012	Hon TANG Ka-piu raised an oral question on Mandatory Provident Fund Schemes	Hansard
5 December 2012	Hon Martin LIAO raised an oral question on Monitoring performance of Mandatory Provident Fund Schemes	Hansard
6 November 2013	Hon CHAN Kin-por raised a written question on Measures to improve the Mandatory Provident Fund Schemes	Hansard