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THE HONG KONG ASSOCIATION OF BANKS
香港銀行公會

Room 525, 5/F., Prince's Building, Central, Hong Kong
Telephone: 2521 1160, 2521 1169 Facsimile: 2868 5035
Email: info@hkab.org.hk Web: www.hkab.org.hk

香港中環太子大廈5樓525室
電話：2521 1160, 2521 1169 圖文傳真：2868 5035
電郵：info@hkab.org.hk 網址：www.hkab.org.hk

21 January 2011

By Post and Email: dsin@legco.gov.hk

Hon CHAN Kam-lam, SBS, JP
Chairman, Bills Committee
Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Bill
C/- Legislative Council Secretariat
Legislative Council Building
8 Jackson Road
Central
Hong Kong

Dear Chairman

Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Bill

Thank you very much for giving us the opportunity to respond to the proposals contained in the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Bill ("**Bill**").

We are pleased to enclose a paper that provides HKAB's comments on the Bill and our suggested refinements, which are based upon a rigorous consideration of the proposals. As we have emphasised in our submission, HKAB fully supports the introduction of the Bill, the consolidation of previous regulatory guidelines and the introduction of a licensing regime for remittance agents and money changers.

HKAB would be delighted to meet with the Bills Committee to discuss the contents of our response further. If you agree that this would be beneficial, we will be pleased to arrange the meeting accordingly.

Yours sincerely

Eva Wong
Secretary

Enc.

Incorporated by Ordinance, Cap. 364
根據條例第364章成立

Bills Committee

Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Bill

Submission of The Hong Kong Association of Banks

21 January 2011

Introduction

This paper sets out the views of The Hong Kong Association of Banks ("**HKAB**") in relation to the proposed introduction of the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Bill ("**Bill**").

HKAB has examined the legislative proposals set out in the Bill and in the explanatory materials and has identified a range of suggestions that we wish to raise with the Bills Committee. These are set out in the "HKAB's response" section of this written submission, with our key suggestions summarised in the "Executive summary".

HKAB's review of the proposals has been led by a committee of 18 HKAB member banks ("**AML Committee**"), involving senior compliance staff and risk practitioners, many of whom specialise in anti-money laundering and counter-terrorist financing ("**AML/CTF**") issues and have significant practical experience in this area.

In addition to the work undertaken during the previous consultation rounds, our review process in relation to the Bill has involved:

1 a comprehensive review of the proposals in the Bill against those that had previously been put forward by the Financial Services and the Treasury Bureau ("**FSTB**") in its second consultation paper dated 7 December 2009 ("**Second Consultation Paper**"), including a review of the way in which HKAB's previous comments have been addressed;

2 an examination of key aspects of the proposals against the approach taken in a sample pool of other jurisdictions, including the European Union, the United Kingdom, Singapore, Australia, New Zealand, the United States and Canada; and

3 discussion among AML Committee members of the following matters, in detail:

   (a) the proposals contained in the Bill;

   (b) our practical experience in dealing with AML/CTF-related issues and complying with the current requirements in the Hong Kong Monetary Authority's ("**HKMA**") Guideline on Prevention of Money Laundering ("**HKMA Guideline**") and related supplement ("**HKMA Supplement**"); and

   (c) relevant standards advocated by international bodies, including FATF and the Basel Committee on Banking Supervision.

HKAB has been assisted in this review process by Mallesons Stephen Jaques.

We would be pleased to engage in further discussions with the Bills Committee in relation to the proposed changes and to provide further industry input where necessary.

Unless otherwise defined, terms used in our response have the meaning given to them in the Bill.

Executive summary

HKAB and its members fully support the introduction of the Bill, the consolidation of previous regulatory guidelines and the introduction of a licensing regime for remittance agents and money changers ("**RAMCs**").

We recognise that it is important that Hong Kong's AML/CTF framework for the financial sector be aligned with international standards, and that legislative reforms take place so as to implement the recommendations proposed by the Financial Action Task Force ("**FATF**") during the mutual evaluation review that it conducted in 2007-08 and in its "40+9" recommendations ("**FATF Recommendations**").

Key refinements sought by HKAB

In summary, HKAB suggests the following key refinements to help ensure that risks are dealt with contextually, that resources are used efficiently and that the requirements are practicable, proportionate and adequately understood by the industry.

1 **Risk-based approach -** The Bill should contain an overarching principle of a risk-based approach, which should be reinforced in relevant provisions of Schedule 2 to the Bill. These adjustments are important to:

(a) accurately reflect the underlying principles of the FATF framework, which requires a sophisticated and contextual approach to the prevention of money laundering and terrorist financing;

(b) ensure that customer due diligence is clearly conceptualised as a process that involves more than a "tick box" approach; and

(c) give financial institutions sufficient latitude to address the circumstances of each case and to direct resources to the areas of greatest risk. This is particularly important given the significant civil and criminal penalties that have been proposed in the Bill.

2 **Implementation -** HKAB understands the need to implement Hong Kong's statutory AML/CTF framework for the financial sector efficiently and to make every effort to implement the regime by mid-2012 to meet FATF's expectations. We are also aware that the current scheduled implementation date is 1 April 2012, as set out in section 1 of the Bill. However, practical guidance and public education is critical to the success of the Bill's implementation. In this regard:

(a) the consultation process for the guidelines that are required to support the Bill should commence as soon as possible. HKAB would also be pleased to render such further assistance that is necessary to help expedite this process;

(b) the Bill should commence at least 12 months after the Bill and all necessary supporting guidelines are in final form. This is essential to allow financial institutions to implement the policies and procedures, and deploy the resources, necessary to comply with the Bill;

(c) the Bill and the supporting guidelines should commence on the same date, to ensure a consistent approach to AML/CTF from the very beginning; and

(d) we ask that the FSTB and relevant authorities undertake a coordinated approach to public education before the commencement of the Bill. We have suggested the specific matters that we believe are important to cover in paragraph 16.2.

3 **Beneficial ownership threshold -** The proposed 10% threshold that has been proposed as part of the tests of ownership of corporations, partnerships and trusts should be adjusted to 25%, in line with the approach taken in other jurisdictions such as the United Kingdom, the European Union and Australia. A threshold of 10% will commercially

disadvantage financial institutions in Hong Kong and create substantial practical difficulties.

4 **Wire transfers and remittance transactions** - The requirements in relation to "wire transfers" and "remittance transactions" should be aligned and merged, on the basis that they have the same economic outcome - value movements - and should be treated consistently from an AML/CTF perspective, irrespective of the type of financial institution that facilitates them. The obligations imposed on an institution receiving an incoming transfer should also be adjusted to:

(a) the risk-based approach advocated by the Basel Committee on Banking Supervision; and

(b) allow post-transaction monitoring. The current proposals exceed the FATF requirements and will significantly impact financial institutions' ability to effect straight-through processing of electronic transfers, and therefore the efficiency of Hong Kong's banking system.

5 **Ongoing due diligence** - In principle, the Bill should impose the same ongoing due diligence standard in relation to both existing and new customers, to facilitate a streamlined compliance approach. The requirements proposed in sections 5 and 6 of Schedule 2 to the Bill should therefore be merged and ongoing due diligence in relation to any customer should be conducted on a risk-sensitive basis and triggered upon a uniform set of trigger events, which should be specified in the unified cross-sectoral guideline.

6 **Correspondent banking** - The correspondent banking-related remediation requirements in section 7 of Schedule 2 to the Bill are unnecessary, because authorised institutions are already subject to stringent due diligence requirements in relation to correspondent banking under paragraph 11 of the HKMA Supplement that mirrors the obligations under FATF Recommendation 7. These requirements have been in effect since 31 December 2004 (with earlier requirements in relation to correspondent banking effected when the original HKMA Supplement was issued on 31 March 2003).

7 **Extraterritorial application** - The provisions extending the application of Schedule 2 to the offshore branches and subsidiary undertakings of locally incorporated financial institutions should be as operationally practicable and realistic as possible. In particular, section 22 of Schedule 2 should be adjusted to:

(a) include a concept of "reasonable steps", in recognition that a financial institution may not have comprehensive control of its offshore operations, even though it may direct its policies and protocols;

(b) extend only to *"majority owned subsidiary undertakings"*, which reflects the approach taken in FATF Recommendation 22;

(c) remove the requirement to take additional measures where a foreign law does not allow an offshore entity to apply the specified measures - this exceeds the requirements of FATF Recommendation 22 and imposes potentially very onerous (and unspecified) requirements on financial institutions;

(d) include a necessary degree of flexibility where it is not reasonably practicable or appropriate for an offshore entity to apply the specified measures; and

(e) empower relevant authorities to issue detailed guidelines to assist financial institutions to comply with the extraterritorial provisions.

8 **Regulation of RAMCs -** The current legislative process provides an excellent opportunity to introduce high standards of conduct in relation to RAMCs that are consistent with those imposed on other financial institutions. HKAB believes that this will strengthen Hong Kong's reputation as a leading international financial market and the perceived integrity of the financial services industry as a whole. A more robust approach (with the enhancements we have suggested in paragraph 24) will also help address the

weaknesses identified by FATF during its mutual evaluation review and create a more commercially equitable playing field.

Supplementary proposals

This paper also describes a number of additional refinements that HKAB considers important for the effective and efficient operation of the new AML/CTF framework. These proposals cover the following key areas:

- the structure of the new framework and the importance of supplementary guidelines;
- the tests of beneficial ownership;
- conducting simplified and ongoing due diligence;
- the special measures applicable to correspondent banking;
- aligning the regulatory treatment of wire transfers and remittance transactions;
- civil pecuniary sanctions and individual criminal responsibility; and
- using the FATF requirements as a benchmark for assessing third parties and jurisdictions.

Practical suggestions

Our response also includes a range of practical recommendations that emanate from HKAB members' substantial collective experience working on AML/CTF-related compliance issues. We have also raised issues that we believe would benefit from further clarification.

Structure of our response

Our comments are grouped into the following thematic categories:

Part A - Key principles

Part B - Customer due diligence measures

Part C - Supervision, investigations and disciplinary actions

Part D - Implementation of the Bill

Part E - Ancillary matters

HKAB would be pleased to discuss any of these matters further with the Bills Committee.

HKAB's response

HKAB supports the introduction of the Bill, the consolidation of previous regulatory guidelines and the introduction of a licensing regime for RAMCs. We recognise that it is important that Hong Kong's AML/CTF system be in line with international standards, and that legislative reforms take place, so as to implement FATF's Recommendations and 2008 mutual evaluation report.

In connection with these legislative proposals, we have identified the following areas of concern that we wish to raise with the Bills Committee.

Part A - Key principles

This part of our response deals with the key principles that HKAB believes are critical to the success of Hong Kong's AML/CTF framework for the financial sector and which are relevant to a number of provisions in the Bill. This part is supplemented by the specific drafting suggestions we have proposed in other parts of our response, as described in the following paragraphs.

1 Risk-based approach

1.1 HKAB fully supports the need for statutory measures in Hong Kong to help prevent money laundering and terrorist financing. We also appreciate that these measures require a contextual approach and that different circumstances present different risks that must be addressed appropriately and efficiently.

1.2 Accordingly, HKAB suggests that the Bill expressly refer to the overarching principle of a risk-based approach. This principle emanates from the FATF Recommendations and FATF has explained its importance as follows:

> *"By adopting a risk-based approach, competent authorities and financial institutions are able to* ***ensure that measures*** *to prevent or mitigate money laundering and terrorist financing* ***are commensurate to the risks identified****. This will allow resources to be allocated in the most efficient ways. The principle is that* ***resources should be directed in accordance with priorities so that the greatest risks receive the highest attention****. The alternative approaches …can inadvertently lead to a 'tick box' approach with the focus on meeting regulatory needs rather than combating money laundering or terrorist financing."*[1] (emphasis added)

1.3 Specifically, HKAB proposes that the following new section be added to Part 2 of the Bill, which introduces the customer due diligence measures. This language reflects FATF Recommendation 5 and similar language that has been adopted by the United Kingdom Money Laundering Regulations.[2]

> ***Risk-based approach***
>
> *A financial institution may determine the extent of the measures described in Schedule 2 on a risk-sensitive basis, depending on the type of customer, business relationship, transaction or other relevant circumstances.*

1.4 HKAB's key reasons for this request are to ensure that:

(a) Hong Kong's statutory regime accurately reflects the principles of the FATF framework. This requires a sophisticated and contextual approach to the prevention of money laundering and terrorist financing;

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1 Paragraph 1.7, Guidance on the risk-based approach to combating money laundering and terrorist financing: High level principles and procedures, June 2007.

2 Regulation 7(3), Money Laundering Regulations (2007).

(b) customer due diligence is clearly conceptualised as a process that involves more than a "tick box" approach, as FATF has emphasised; and

(c) financial institutions have sufficient latitude to address the circumstances of each case and to direct resources to the areas of greatest risk. This is particularly important given the significant civil and criminal penalties that have been proposed in the Bill.

1.5 In connection with this proposal, HKAB also suggests that relevant provisions in Schedule 2 reinforce the principle of a risk-based approach. Please refer to annexure 1 for our suggested drafting.

2 Structure of the Hong Kong framework

2.1 The Bill contains a number of provisions that enable relevant authorities to issue guidelines about the operation of certain aspects of the Bill (including customer due diligence measures). HKAB supports this approach and agrees that supplementary guidelines are essential for providing practical assistance on AML/CTF issues.

2.2 HKAB also believes that the Hong Kong framework should be structured in a principled way, to ensure that it is as effective as possible and is consistently applied. In particular, we are eager to ensure that Hong Kong's new framework:

(a) allows sufficient flexibility to address the myriad of circumstances that may arise in day-to-day practice, as well as future AML/CTF-related developments;

(b) maximises consistency across sectors and does not inadvertently impose requirements upon one type of financial institution that are more onerous than, or inconsistent with, those imposed upon another;

(c) assists financial services groups that include different types of financial institutions (eg banks, securities firms and insurances companies) to adopt consistent internal protocols; and

(d) gives relevant authorities sufficient power to address the particular risks faced by the financial institutions they regulate.

2.3 In this regard, we suggest that:

(a) the Bill contain the core framework for Hong Kong's new AML/CTF regime for the financial sector, including key due diligence requirements, principles (such as the risk-based approach we have described in paragraph 1) and ancillary provisions;

(b) the practical requirements that flesh out this framework be set out in non-statutory guidance, contained in two tiers of guidelines:

(i) a cross-sectoral guideline ("**Unified Guideline**") that is issued by all relevant authorities (or the Secretary for Financial Services and the Treasury), which contains practical requirements that apply to all financial institutions and interpretative guidance on key concepts used in the Bill; and

(ii) sector-specific guidelines ("**Sectoral Guidelines**") issued by a single relevant authority (eg the Hong Kong Monetary Authority) that address the needs of specific categories of financial institutions (eg banks) and provide additional examples of how the Bill and the Unified Guideline should be applied; and

(c) the enabling provisions in the Bill be strengthened to ensure that relevant authorities have sufficient power to enact these guidelines. We also suggest that the Secretary for Financial Services and the Treasury also be empowered to issue guidelines under section 7 of the Bill.

2.4 Our specific suggestions to help implement this framework are detailed in:

(a) annexure 2, which describes the matters that we suggest including in the Unified Guideline and the Sectoral Guidelines and our suggested drafting changes to the current enabling provisions; and

(b) other relevant sections in the main body of our response, in connection with our comments on specific proposals in the Bill. These suggestions are also summarised in annexure 2.

2.5 We also refer the Bills Committee to our comments about implementation timing in paragraph 15.

3 Benchmarks: assessing other jurisdictions and third parties

3.1 A number of provisions in the Bill require financial institutions to assess the requirements imposed by a country, or the standards to which a third party is subject, against the due diligence measures in Schedule 2 to the Bill. For example, the definition of "equivalent jurisdiction" in section 1 of Schedule 2 to the Bill includes *"a jurisdiction that imposes requirements similar to those imposed under this Schedule [2]"*.

3.2 HKAB understands the need for benchmarking to ensure the integrity of Hong Kong's controls and we also recognise that its inclusion in the Bill reflects Hong Kong's responsibilities as a FATF member. However, we have the following three suggestions that we believe will help improve this benchmarking approach.

(a) First, we ask that the benchmark used in the Bill be adjusted to refer to the FATF Recommendations, instead of Schedule 2. The reasons for this request are that:

(i) the FATF Recommendations contain the internationally-recognised principles with which FATF members are expected to comply;

(ii) the customer due diligence measures in the Bill adopt the FATF Recommendations contextually - that is, they have been adjusted to address the needs of the financial sector in Hong Kong. This means that they may not be relevant to other jurisdictions or other parties; and

(iii) linked to paragraph (ii), the level of specificity in the Bill is currently greater than the FATF Recommendations, making the benchmarking process more onerous and raising the likelihood that additional inconsistencies will arise. We suggest that these types of implementation-related inconsistencies should not be relevant if the underlying principles are consistent with the FATF framework.

The specific provisions that this request affects (and our suggested drafting) are set out in annexure 3. We would be pleased to discuss the issue further with the Bills Committee.

(b) Second, we suggest that the test of "similarity" between the requirements imposed by the relevant benchmark and those adopted by an offshore entity be adjusted to a test of "broad equivalence". This formulation is used in the New Zealand AML/CTF rules[3] and we suggest that it provides the necessary flexibility to reflect that each country takes a unique approach to AML/CTF to address its own needs, and to avoid rigid comparisons.

(c) Third, we request that the Financial Services and the Treasury Bureau (or another appropriate body) provide a list of jurisdictions that it considers to be "equivalent jurisdictions". This mirrors the approach taken by the United Kingdom in the "paper on equivalence" issued by the Joint Money Laundering

[3] Section 61, Anti-Money Laundering and Countering Financing of Terrorism Act 2009.

Steering Group (with input from Her Majesty's Treasury).[4] It will assist in ensuring a consistent industry approach (to help avoid differential treatment by each individual financial institution) and the efficient use of resources, including minimising external legal costs. We also ask that this list either be included in, or incorporated by reference into, the Unified Guideline.

(d) Fourth, we ask that the Unified Guideline contain specific guidance on how financial institutions should assess (i) other jurisdictions that may not appear on the list we have requested in paragraph (c); and (ii) third parties (and their respective standards) against the FATF Recommendations. In this regard, we suggest that the Unified Guideline also include a list of criteria and the types of deviations that are acceptable.

3.3 Related to the issue of benchmarking, HKAB would also be grateful if the Administration could please clarify its expectations about the way that financial institutions should treat FATF member countries that have been identified by FATF as non-compliant. That is, HKAB would like to understand if this would affect a country's status as an "equivalent jurisdiction" for the purposes of the Bill.

Part B - Customer due diligence measures

This part of our response contains HKAB's comments on Schedule 2 to the Bill. We also refer the Bills Committee to Part E of our response, which contains additional supplementary points that are also relevant to customer due diligence.

4 Beneficial ownership - overall approach

4.1 Section 1 of Schedule 2 describes the "beneficial owner" in relation to particular types of customers for the purpose of the due diligence requirements in Schedule 2.

4.2 HKAB suggests that this definition be generalised to match the FATF Recommendations, which define "beneficial owner" qualitatively,[5] and that the precise tests of ownership be detailed in the Unified Guideline. This request reflects:

(a) our suggestion in paragraph 2 that the Bill contain the core principles of Hong Kong's AML/CTF framework, with details and guidance contained in supplementary guidelines;

(b) that the specific tests that apply to a particular type of customer require sufficient flexibility to adapt to different situations (for example, where it is not practicable to ascertain the protector or enforcer of a trust) and practical guidance. We suggest that the tests, guidance and alternative measures should be grouped together in the Unified Guideline to facilitate efficient compliance; and

(c) that even on the current drafting of this definition in the Bill, we suggest that guidance is required to explain the meaning of "ultimate control". Placing all the specific tests into one document will therefore streamline the drafting approach.

4.3 Specifically, we suggest that the definition of "beneficial owner" in the Bill be simplified so that it reads as follows:

> ***beneficial owner*** *(實益擁有人)—*
>
> *(a) in relation to a customer that is corporation or a partnership, means an individual who exercises ultimate control over the management of that corporation or partnership;*

[4] Contained in section 2, "Prevention of money laundering / combating terrorist financing: Guidance for the UK Financial Sector, Part III: Specialist Guidance", October 2010.

[5] Glossary to the FATF Recommendations.

(b) in relation to a trust, means an individual who has ultimate control over the trust; or

(c) in relation to a customer not falling within (a) or (b), means:

(i) an individual who ultimately owns or controls the customer; or

(ii) if the customer is acting on behalf of another person, the other person.

4.4 We have used the words "in relation to a trust" in this proposal rather than the current drafting in the Bill (*"in relation to a customer that is a trust"*) because we suggest that it is more appropriate - the financial institution's "customer" would technically be the trustee acting on behalf of the trust.

4.5 HKAB's additional comments in relation to the specific tests of beneficial ownership that have been proposed in the Bill (and which we have suggested be shifted into the Unified Guideline) are set out in the following paragraph 5.

5 Beneficial ownership - specific tests

5.1 In relation to corporations, partnerships and trusts, a 10% threshold has been proposed in the definition of "beneficial owner" as part of the tests of ownership. For example, the beneficial owner of a corporation is defined to include a person entitled to exercise or control at least 10% of voting rights at its general meetings.[6]

5.2 HKAB asks that as a general principle, this threshold be adjusted to 25%, noting that the FATF Recommendations only define "beneficial owner" qualitatively (without a percentage ownership threshold)[7] and the approach in other jurisdictions is to apply a 25% standard. For example, Australia,[8] the United Kingdom[9] and the European Commission[10] each impose a 25% threshold.

5.3 HKAB members are concerned that if the existing 10% threshold is retained, Hong Kong financial institutions will:

(a) be commercially disadvantaged when dealing with customers who are not subject to equivalent evidentiary requirements in other FATF member jurisdictions; and

(b) face a substantial practical burden of conducting due diligence. For example, a number of HKAB members already face practical obstacles in relation to complying with the current due diligence requirements in the HKMA Supplement in relation to holders of 10% or more of the voting rights in a company.[11] For example, some members have experienced difficulty obtaining reliable information about 10% shareholders from company information providers in foreign jurisdictions that apply a 25% test.

5.4 HKAB is not aware of the background to the 10% threshold proposed in the Bill. For example, we are not aware if this proposal was based on a specific risk assessment

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6 Currently proposed in section 1(1) of Schedule 2 to the Bill (paragraph (a)(ii) of the definition of "beneficial owner").

7 Glossary to the FATF Recommendations.

8 Definition of "Beneficial Owner" in section 1.2 of the Anti-Money Laundering and Counter-Terrorism Financing Rules Instrument 2007 (No.1).

9 Regulation 6 of the Money Laundering Regulations 2007 (United Kingdom).

10 Article 3(6), Third European Union Money Laundering Directive (2005/60/EC of the European Parliament and of the Council of 26 October 2005). In the case of corporations, the test is 25% plus one share: Article 3(6)(a)(i).

11 Paragraph 13, Interpretative Notes to the HKMA Supplement.

performed by the Administration. We therefore welcome further discussion on this point, if required.

5.5 In relation to corporations specifically (paragraph (a) of the definition of "beneficial owner"), please also refer to our comments in annexure 2.

6 Simplified customer due diligence

6.1 We suggest that state-owned enterprises and their subsidiaries should enjoy the benefit of simplified customer due diligence. This would be consistent with paragraph 4.2 of the HKMA Supplement, which states:

> *"Where a customer is a company which is listed on a recognised stock exchange…or is a state-owned enterprise or is a subsidiary of a listed company or state-owned enterprise, the customer itself can be regarded as the person whose identity is to be verified. It will therefore generally be sufficient for an [authorised institution] to obtain and retain sufficient information to effectively identify and verify the identity of the customer…, the natural persons appointed to act on behalf of the customer and their authority to do so…."*

6.2 To implement this suggestion, we suggest that a new reference to such entities be added to section 4(2) of Schedule 2 to the Bill. We appreciate that state-owned entities could fall within the scope of section 4(2)(f), but we think that an express reference is important for clarity. This also ties into our suggestions in relation to clarifying the definition of "public body" in paragraph 20.

6.3 HKAB also suggests that section 4(6) of Schedule 2, which allows simplified due diligence in relation to solicitors' mingled accounts, be expanded to other designated non-financial businesses and professions specified by the FATF Recommendations,[12] such as accountants and accounting firms. However, we appreciate that not all such designated non-financial entities are subject to comprehensive AML/CTF-related regulatory controls in Hong Kong. In this regard, if the Administration does not believe that such an expansion is currently appropriate, we ask that a new subsection be added to section 4 of Schedule 2 after subsection (6), to facilitate future development. We suggest the following drafting:

> The Secretary for Financial Services and the Treasury may designate additional circumstances in which a financial institution may undertake simplified customer due diligence, and the measures that must be undertaken in those circumstances, by notice published in the Gazette.

6.4 HKAB suggests that the Bill complement the simplified customer due diligence procedures with a provision similar to paragraph 4.6 of the HKMA Supplement. In particular, we suggest that where:

(a) simplified due diligence is permitted in relation to a person under section 4(2) of Schedule 2 to the Bill; and

(b) that person forms part of the ownership chain of another person,

section 4 of Schedule 2 to the Bill specify that it is generally sufficient for the financial institution to verify the identity of the first person in accordance with section 4(1) of Schedule 2.

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[12] Glossary to the FATF Recommendations, which we suggest be used as a guide only.

6.5 HKAB also has the following ancillary points in relation to the simplified due diligence rules in section 4 of Schedule 2 to the Bill.

(a) We suggest that the term "subsidiary" be defined for the purposes of section 4 of Schedule 2. We suggest that this could be achieved by shifting the definition of this term in section 17 of Schedule 2 (which cross-refers to the definition in the Companies Ordinance (Cap. 32)) to section 1(1) of Schedule 2.

(b) We also suggest that section 4(7) of Schedule 2 to the Bill be adjusted by adding a definition of "stock exchange" for the purpose of section 4(2)(c) of Schedule 2. We recommend that this term be defined in the same way as that term is defined in Part 1 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571) ("**SFO**").

(c) We would also be grateful for clarification as to whether the reference to a "pension scheme" in section 4(4)(b) of Schedule 2 is intended to be interpreted narrowly, or should be read more broadly by reference to section 4(4)(a), which refers to "provident, pension, retirement or superannuation scheme (however described)".

7 Wire transfers and remittance transactions

7.1 HKAB has concerns about the conceptual and regulatory distinction that has been drawn in the Bill between "wire transfers" (defined in section 1(4) of Schedule 2) and "remittance transactions" (defined in section 13 of Schedule 2), which we believe is unnecessary and inappropriate. In particular:

(a) we believe that these transactions ultimately have the same outcome - value movements. We suggest that they should therefore be treated consistently from an AML/CTF risk mitigation perspective, irrespective of the type of financial institution that facilitates them;

(b) there is no such distinction in the FATF framework, which uses derivations of these terms interchangeably (for example, Special Recommendation VII deals with "money remitters" in the context of "wire transfers");[13]

(c) the due diligence and monitoring requirements for remittance transactions are weaker than those imposed on wire transfers, and the concept of "remittance transaction" does not include domestic transfers; and

(d) we understand that some industry participants in Hong Kong currently draw a distinction between "remittances" and "transfers" to avoid complying with regulatory obligations imposed on remittances - HKAB suggests that applying a uniform concept in the Bill will help ensure that similar distinctions between concepts are not made.

7.2 Our specific suggestions to address these concerns are:

(a) that a uniform concept of "money transfer" replace the concepts of "wire transfer" and "remittance transaction". We believe that this term clearly describes the concept and helps prevent confusion and avoidance. We suggest that it can be defined in section 1 of Schedule 2, in the same way as "remittance transaction" is currently defined - that is:

> *"…a transaction for— (a) sending, or arranging for the sending of, money to a place outside Hong Kong; (b) receiving, or arranging for the receipt of, money from a place outside Hong Kong; or (c) arranging for the receipt of money in a place outside Hong Kong"*;

[13] Paragraph VII, FATF Special Recommendation VII: Wire transfers.

(b) the amendment of section 12 of Schedule 2 so that it refers to money transfers rather than "wire transfers". Please refer to annexure 4 for our suggested drafting; and

(c) the deletion of section 13 of Schedule 2.

7.3 The drafting adjustments shown in annexure 4 also include:

(a) a request that the obligations imposed on a beneficiary institution (that is, an institution receiving an incoming transfer) be adjusted to mirror the current risk-based approach in paragraph 9.7 of the HKMA Supplement, which also allows post-transfer monitoring.[14] Our reasons for this request are that:

(i) it is not always technically possible to refuse an incoming transfer - for example, electronic transfers received by banks are often automatically credited to a customer's account without an opportunity for the bank to "refuse" the transfer - this would make complying with the obligations imposed on beneficiary institutions in sections 12(9) and (10) impossible in practice and significantly impact financial institutions' ability to effect straight-through processing; and

(ii) it reflects the risk-based approach advocated in the Basel Committee on Banking Supervision's paper on 'Due diligence and transparency regarding cover payment messages relating to cross-border wire transfers';[15] and

(b) more general drafting proposals that we suggest will enhance the operation of the transfer provisions.

7.4 If the Administration does not agree with these proposals and wishes to retain the two different concepts, HKAB:

(a) would be very grateful for additional guidance on the Administration's reasons for this approach, the conceptual difference that is intended to be drawn between the two concepts and the criteria that should be used to distinguish them; and

(b) suggests that section 3(1)(c) of Schedule 2, which concerns due diligence on occasional transactions, be amended as follows to align the standards imposed on money transfers, irrespective of the way that they may be carried out or by whom:

> *"Subject to section 4 of this Schedule, a financial institution must carry out customer due diligence measures in relation to a customer in the following circumstances—*
>
> *…..*
>
> *(c) despite paragraph (b) [which requires due diligence on occasional transactions ≥ $120,000], before carrying out for the customer an occasional transaction that is a wire transfer or a remittance transaction involving an amount equal to or above $8,000 or an equivalent amount in any other currency, whether the transaction is carried out in a single*

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[14] Paragraph 9.7 states the following: *"An [authorised institution] handling incoming wire transfers for a beneficiary should conduct enhanced scrutiny of, and monitor for, wire transfer messages which do not contain complete originator information. This can be done through risk-based methods taking into account factors that may arouse suspicion (e.g. country of origin of the wire transfer). If necessary, this may be done after effecting the transaction particularly for items handled by straight-through processing."*

[15] Published in May 2009. A copy of the full text of the final paper can be found at www.bis.org/publ/bcbs154.pdf. See particularly paragraph 32 in relation to the risk-based approach suggested for beneficiary institutions.

operation or in several operations that appear to the financial institution to be linked…"

(c) requests that its other proposals in relation to section 12 of Schedule 2 that are described in annexure 4 (that is, the proposals that do not relate solely to merging the two concepts) be considered by Bills Committee;

(d) notes that the exceptions for principal-to-principal wire transfers in section 12 of Schedule 2 are not relevant because "wire transfer" is defined as transactions carried out "on behalf of a person"; and

(e) recommends that section 13 of Schedule 2:

(i) be strengthened so that it includes obligations on par with section 12 of Schedule 2 - in particular, it should include requirements to record information in relation to bundled remittance transactions and to monitor incoming remittance transactions on a risk-sensitive basis; and

(ii) if this approach is not taken, be adjusted to make clear that these due diligence requirements only apply where the money service operator is taking orders from the originator - this is required because this section refers to "carrying out a remittance transaction" and a "remittance transaction" is defined to include both sending and receiving money. We suggest that the current drafting would produce an unusual result (requiring the recipient institution to verify the originator's identity).

7.5 If adopted, we appreciate that the suggestions we have made in this paragraph 7 may require drafting adjustments, which will depend on the approach chosen by the Administration. To the extent that we have not already covered these points in annexure 4, HKAB would be pleased to provide additional drafting suggestions if required.

8 Pre-existing customers and ongoing due diligence

8.1 HKAB suggests that in principle, the Bill impose the same ongoing due diligence standard in relation to both existing and new customers. That is, we suggest that the Bill merge the requirements in sections 5 and 6 of Schedule 2 to the Bill and that ongoing due diligence in relation to *any* customer be triggered upon a uniform set of trigger events.

8.2 Our reason for this request is to facilitate a streamlined compliance approach. Treating all customers consistently will ensure that the circumstances when ongoing due diligence is required are clearly understood. The combined effect of the current proposals is that a financial institution would need to verify whether a customer was onboarded before the commencement of the Bill before determining which ongoing due diligence requirements should apply. HKAB suggests that this is impracticable and unnecessary.

8.3 To implement this request, we suggest that:

(a) section 5 of Schedule 2 to the Bill be adjusted so that it applies to both new and existing customers. Please refer to annexure 5 for our specific drafting suggestions, which include adjustments to reflect the terminology used in the FATF Recommendation 5; and

(b) section 6 of Schedule 2 be deleted and the trigger events in that section be shifted into the Unified Guideline to describe the "appropriate times" that due diligence should be conducted for the purposes of section 5 of Schedule 2 to the Bill.

8.4 In our comments in annexure 5, we have also asked that the reference to additional ongoing due diligence measures in relation to customers who were not physically present

for identification purposes[16] be deleted. We agree that not being physically present for identification is relevant to onboarding, which is covered in section 9 of Schedule 2. However, we suggest that it is not relevant to the relationship as a whole, in the absence of any other circumstances suggesting an elevated risk of money laundering or terrorist financing. A number of HKAB members are also concerned that the imposition of more onerous responsibilities in relation to such customers throughout the course of the relationship would lower their competitiveness in the region, particularly given the number of non face-to-face relationships in Hong Kong.

8.5 HKAB would also be grateful for the following clarifications in relations to the triggers for ongoing due diligence.

(a) First, the trigger currently proposed in section 6(1)(b) of Schedule 2 to the Bill requires a review of customer documentation when:

> *"the financial institution becomes aware that, having regard to its current documentation standards, it lacks sufficient information about a customer"*.

HKAB supports the adoption of a general ongoing due diligence trigger event and we acknowledge that it reflects an existing requirement to which HKAB members are subject.[17] However, we suggest that the Unified Guideline clarify that it only applies to customers in relation to whom a financial institution has already conducted due diligence under the new regime. Otherwise, the trigger event should technically occur for all pre-existing customers as soon as the Bill is implemented, because all financial institutions will be required to change their documentation standards.

This requested clarification is also consistent with the FSTB's comments in its Second Consultation Conclusions that *"the statutory requirement… should be triggered only upon [the] occurrence of specified events which will be prescribed in the new legislation"*[18] - rather than the implementation of the Bill itself.

(b) Second, HKAB requests that the Unified Guideline contain guidance explaining:

(i) transactions that are "complex, unusually large in amount or of an unusual pattern" and which have "no apparent economic or lawful purpose" for the purpose of section 5(1)(c) of Schedule 2 to the Bill. We suggest that this include examples that are relevant to different types of institutions and cover a range of domestic and offshore circumstances;

(ii) when a "material change occurs in the way in which the customer's account is operated" for the purpose of the trigger event currently proposed in section 6(1)(c) of Schedule 2;

(iii) what will constitute sufficient "additional measures" for the purpose of section 5(3) of Schedule 2 to the Bill, to assist financial institutions manage their compliance resources. The FSTB recognised this need during its consultation on the new framework, stating that the compliance costs associated with these reviews should be minimised as far as reasonably practicable;[19] and

(iv) the precise types of information that should be re-reviewed and when this should be done.

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16 Section 5(3)(a), Schedule 2 to the Bill.

17 Section 12.3, HKMA Supplement.

18 Paragraph 15, Second Consultation Paper conclusions.

19 Paragraph 2.4(b), first consultation paper issued by the FSTB on 9 July 2009.

9 Correspondent banking

9.1 HKAB asks that section 7 of Schedule 2, which imposes remediation requirements on members in relation to pre-existing correspondent banking relationships, be deleted.

9.2 Our reasons for this request are that:

(a) this section only applies to authorised institutions supervised by the HKMA. Authorised institutions are already subject to due diligence requirements in relation to correspondent banking under paragraph 11 of the HKMA Supplement that mirror the obligations under FATF Recommendation 7. These requirements have been in effect since 31 December 2004 (with earlier requirements in place since the original HKMA Supplement was issued on 31 March 2003);

(b) the obligations in section 7 are, in effect, required to be performed before the Bill comes into effect. This is because any relationship that does not meet the requirements must be terminated "on the date of commencement of [the] Ordinance".[20] HKAB suggests that this contravenes the principle against legislative retrospectivity because it contains statutory requirements that pre-date the Bill's implementation;

(c) linked to paragraph (b), the requirement to terminate a non-conforming correspondent banking relationship in section 7(2) of Schedule 2:

(i) has immediate effect upon the Bill's commencement (which may be 1 April 2012 or any other specified date), contrary to the Administration's Background Brief to the Bills Committee, which stated that:

> *"there would be a reasonable lead time between the enactment and commencement of the legislation to allow financial institutions to enhance their internal control system and procedures for compliance with the new legislation. The relevant regulatory authorities would also organize workshops and seminars to facilitate financial institutions to familiarize with the new legislation"*;[21] and

(ii) is a "specified provision" under section 5(10) of the Bill. This means that a failure to comply with it carries potential criminal liability under sections 5(5) to 5(9) of the Bill and possible regulatory sanctions under section 21 of the Bill. HKAB suggests that when combined with the immediate effect of section 7(2) of Schedule 2, these sanctions are unfair; and

(d) we believe that it is more appropriate that section 14 of Schedule 2, which contains the general correspondent banking due diligence requirements, uniformly regulate those relationships and that any perceived deficiencies in current practice be remedied in consultation with the HKMA.

9.3 In relation to the general correspondent banking due diligence requirements in section 14 of Schedule 2, we have the following additional comments.

(a) First, we ask that the requirement that an authorised institution have "documented its responsibilities and the responsibilities of the proposed respondent bank"[22] be retained in non-statutory guidance issued by the HKMA (that is, in a new Sectoral Guideline once the Bill is implemented) and deleted from section 14 of Schedule 2 to the Bill.

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20 Section 7(2) of Schedule 2, Bill.

21 Appendix, point (g) to the Background Brief for the Bills Committee (LC Paper No. CB(1) 595/10-11).

22 Section 14(2)(c) of Schedule 2, Bill.

Our reason for this request is that the current industry practice is to conduct a gap analysis between the steps taken by the respondent bank and the responsibilities of the authorised institution, so that the authorised institution understands what it needs to do to comply with its AML/CTF obligations. The requirement to "document" responsibilities therefore requires a contextual understanding of the way in which the parties' respective responsibilities are understood and internally recorded. We suggest that the HKMA is best placed to assess compliance with this requirement, bearing in mind that section 14 applies only to authorised institutions and that the HKMA has already been supervising compliance with this requirement since December 2004.[23]

(b) Second, we suggest that a Sectoral Guideline issued by the HKMA provide additional practical guidance on correspondent banking, similar to the Wolfsberg Group's "Anti-Money Laundering Principles for Correspondent Banking" and related FAQs, which contains standards and practical guidance on managing risks associated with correspondent banking. In particular, HKAB would appreciate non-statutory guidance on:

(i) the sort of evidence that an authorised institution can rely upon in relation to a proposed respondent bank (for example, a certificate, or public records that show that it is incorporated or established in an equivalent jurisdiction);

(ii) the methods of assessing a proposed respondent bank's AML/CTF controls and whether an authority has "functions similar to those of the [HKMA]"; and

(iii) the types of accounts that are contemplated by section 14(2) of Schedule 2, which are directly operable by a customer.

9.4 Our suggestions in relation to section 14 of Schedule 2 also apply to section 7 if, contrary to our request, that provision is retained. We also suggest that those provisions be merged for the sake of drafting efficiency.

10 Other high risk situations

10.1 HKAB suggests that section 15 of Schedule 2 to the Bill be adjusted as follows:

> A financial institution must, in a situation specified by the relevant authority in a notice in writing given to the financial institution and in any other situation that by its nature may present a high risk of money laundering or terrorist financing, take reasonable additional measures to mitigate that risk, on a risk-sensitive basis.~~—~~
>
> ~~(a) obtain approval from its senior management to establish or continue the business relationship concerned; and~~
>
> ~~(b) take adequate measures to establish the relevant customer's or beneficial owner's source of wealth and the source of the funds that will be or are involved in the business relationship concerned.~~

10.2 Our reason for this suggestion is to ensure that this provision provides sufficient flexibility for relevant authorities and financial institutions to determine the measures that are appropriate for a given high risk situation. For example, we suggest that establishing a customer's source of wealth will not be relevant (or helpful) in all cases and may therefore result in the unnecessary expenditure of resources.

10.3 We have also suggested that the concept of "reasonable measures" be used (rather than "adequate measures"), because it is the terminology used in the FATF Recommendations and expresses the concepts of relevance and proportionality.

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[23] The current requirement is contained in paragraph 11.3, HKMA Supplement.

10.4 To complement these adjustments, we suggest that both the Unified Guideline and Sectoral Guidelines contain non-statutory guidance that provide examples of high risk situations and the measures that may be appropriate to mitigate those risks. This would be consistent with the approach taken in the current HKMA Supplement, which provides examples of "high risk or sensitive customers".[24]

10.5 Please also refer to our comments in paragraph 18 about customers who are not physically present for identification purposes paragraph 19 about politically exposed persons, which flow from our suggestions and observations in this paragraph 10.

11 The obligation to implement measures and procedures

11.1 HKAB members are concerned about the additional obligations imposed on financial institutions under section 23 of Schedule 2 to the Bill. This requires a financial institution to *"take all reasonable measures- (a) to ensure that proper safeguards exist to prevent a contravention of any requirement under Part 2 or 3 of this Schedule; and (b) to mitigate money laundering and terrorist financing risks"*.

11.2 In particular, we believe that this requirement is superfluous because the operative requirements in the Bill inherently require financial institutions to take appropriate measures to ensure compliance. We are also concerned about its breadth and lack of specificity. This is especially concerning, having regard to the possibility of criminal sanctions for a failure to comply with this section, even where there may not be any actual breach of the due diligence requirements in the Bill. We also observe that the FATF Recommendations do not include an equivalent requirement.

11.3 To address these concerns, we request that section 23 of Schedule 2 be deleted from the Bill, because we suggest that it is more appropriate that:

(a) the adoption of appropriate policies and procedures to comply with Hong Kong law fall within the purview of a financial institution's primary regulator;

(b) financial institutions only be exposed to criminal liability where an actual compliance failure has occurred (with the necessary *mens rea*); and

(c) any perceived weaknesses in compliance policies and procedures be addressed through the broad powers granted to relevant authorities when dealing with actual compliance failures, under section 21 of the Bill (which is required to be supported by important interpretative guidance issued under section 23 of the Bill).

11.4 If the Administration does not agree with this request, we ask that the Bills Committee consider addressing the concerns we have raised by:

(a) shifting the requirement into Sectoral Guidelines (reflecting the current approach)[25] or, alternatively, removing the reference to section 23 of Schedule 2 to the Bill from the list of "specified provisions" in section 5(10) of the Bill; and

(b) clarifying the Administration's expectations in relation to the measures that financial institution is required to implement, by:

(i) including more specific criteria in section 23 of Schedule 2 to the Bill; or

(ii) requiring each relevant authority to issue a Sectoral Guideline that contains the criteria that will satisfy the principles of "reasonable measures" and "proper safeguards" (for example, by adding a new section 24 to Schedule 2 that mirrors section 23 of the Bill).

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[24] For example, paragraphs (e) and (i), Annex 2, Interpretative Notes, HKMA Supplement.

[25] Paragraph 16.2, HKMA Supplement.

11.5 Our comments in relation to section 23 of Schedule 2 to the Bill also apply, in substance, to section 19 of Schedule 2. In particular, we also request that section 19 of Schedule 2 be deleted or that our concerns in relation to criminal liability and specificity be addressed as suggested in paragraph 11.4. Should both provisions be retained, contrary to our request, we ask that the Unified Guideline provide clear guidance as to the interaction of the two provisions.

Part C - Supervision, investigations and disciplinary actions

This part of our response contains HKAB's comments on Parts 3 and 4 of the Bill.

12 Investigation and inspections

12.1 HKAB understands the need for the regulatory powers of inspection and investigation in Part 3 of the Bill, and we appreciate the efforts that have been made to align the new requirements with similar provisions in the SFO.

12.2 To support the transparency and integrity of this regime, HKAB has a small number of requested adjustments to Part 3, as follows.

(a) We ask that a relevant authority's power to authorise a person to enter a financial institution's premises under section 9 of the Bill be limited to circumstances where:

(i) a magistrate has approved that authorisation, which we suggest be incorporated as a mandatory condition precedent to the exercise of the powers proposed in sections 9(1) and 9(12) of the Bill (with an equivalent condition precedent also adopted for the purpose of investigations under sections 11 and 12 of the Bill); and

(ii) there are reasonable grounds to do so, similar to the approach on investigations in section 12 of the Bill, to minimise the potential disruption to normal business operations. Specifically, we suggest the following drafting adjustments to section 9 of the Bill:

> (1) Where a relevant authority has reasonable cause to suspect that a financial institution ~~For the purpose of ascertaining whether a financial institution~~ is not complying or has not complied with, or is not likely to be able to comply with, the requirement specified under subsection (2), an authorized person may at any reasonable time—

(b) We also ask that, as a matter of fairness, requests for information under sections 9(3) and 9(5) be made by written notice, and include supporting details and a reasonable period to provide that information. To help address any concerns that this might impede the inspection process, we acknowledge that the need for an appropriate exception to this notice requirement. Our suggested drafting for a new subsection is as follows:

> An authorized person may only exercise the powers in subsections (3) and (5) to require a person to answer questions by providing a written notice specifying-
>
> (a) the questions required to be answered;
>
> (b) the reasons for the request for information;
>
> (c) the manner in which the person must provide their answers;
>
> (d) a reasonable period of time within which the answers must be provided; and

> (e) the consequences of failing to respond to the questions.
>
> An authorized person is not required to comply with this subsection [*] where the relevant authority is satisfied, and has certified in writing that it is satisfied, that complying with this subsection [*] would materially prejudice the purposes of this section.

(c) We also suggest that the HKMA's consent be required in relation to the disclosure of any customer-related information in any case where the HKMA is not the relevant authority that is requesting information under section 9. This reflects the sensitivity of customers' banking-related information and authorised institutions' obligations of confidence under their regulatory duties and the general law. Our suggested changes to section 9(8) to address this request are as follows. This comment also applies to section 12.

> If an authorized person is authorized under subsection (12) by a relevant authority other than the Monetary Authority, this section is not to be construed as requiring an authorized institution, not being the financial institution as referred to in subsection (1), to disclose any information or produce any record or document relating to the affairs of a customer to the authorized person unless the relevant authority is satisfied, and certifies in writing that it is satisfied, that the disclosure or production is necessary for the purposes of this section and the Monetary Authority has given its prior consent in writing to that disclosure.

12.3 We ask that section 9(14) be amended so that a person's authorisation must be produced before exercising a statutory power of inspection. We suggest the following specific drafting changes:

> Before ~~When~~ exercising a power under this section, an authorized person must ~~as soon as reasonably practicable~~ produce a copy of the relevant authority's authorisation for inspection.

12.4 In relation to the definition of "business premises" in section 9(15), we ask that:

(a) the inspection rights in section 9:

(i) only extend to premises in Hong Kong; or

(ii) in the alternative, be subject to all applicable local laws and regulatory requirements in any place outside Hong Kong. For example, it is possible that consent may be required from regulators in other jurisdictions; and

(b) the scope of authorised institutions' premises caught by these inspection provisions be narrowed. For example, HKAB would like to understand the rationale for including places of business that are specifically declared not to be a "local office".[26] We suggest that it would be more appropriate that the inspection rights only concern the business premises of an authorised institution that are required to be approved by, or notified to, the HKMA.

12.5 HKAB requests that the double jeopardy safeguards in section 10(10) of the Bill also extend to criminal proceedings under section 13 and under other relevant industry laws, such as section 180 of the SFO (which contains the inspection rights of persons authorised by the Securities and Futures Commission ("**SFC**") and the HKMA). We suggest that it is reasonably foreseeable that criminal proceedings in respect of the same

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[26] Paragraph (a)(iv) of the definition of "business premises" in section 9(15) of the Bill.

conduct could be instituted under all of these provisions. We also re-iterate this request in relation to the similar double jeopardy safeguards in sections 13(10) and 14(4), with the relevant adjustments.

12.6 Section 14 of the Bill allows an authorised person or investigator to apply to the Court of First Instance for an inquiry into why a person has failed to comply with a relevant inspection or investigation requirement. If the Court finds that there was no reasonable excuse for the failure, it may require the person to comply with the requirement and punish the person (and anyone else knowingly involved) as if it were a contempt of court. While HKAB understands that this drafting mirrors section 185(1) of the SFO, we ask that the Bills Committee consider adjusting this provision so that punishments only apply where the person has failed to comply with an order made by the Court under section 14(2)(a). We suggest that this is a fair and reasonable approach, bearing in mind the broad range of other penalties that could apply to the failure.

12.7 Finally, HKAB would also appreciate if the Administration could please clarify:

(a) whether a person has the right to refuse to answer a question posed under section 9 on the grounds that to do so might tend to incriminate them (the commentary in the Second Consultation Paper seems to indicate that this was not intended).[27] The investigation-related requirements in section 13 explicitly say that they cannot, and if that is also the case for section 9, we ask that the provisions be aligned for consistency;

(b) if a person can refuse to comply with a request made under section 9 of the Bill for a record or a document on the grounds that they do not possess it (which constitutes grounds for a refusal under section 12(5) of the Bill, which relates to investigations). If so, we ask that section 9(10) be aligned with the approach in section 12(5);

(c) in relation to sections 10(7), 10(8), 13(7) and 13(8) of the Bill:

(i) the difference between "employee" and "employed to work for a financial institution"; and

(ii) the meaning of a person "concerned in the management of a financial institution."

We suggest that as an alternative, and in the interests of regulatory consistency and clarity, the Bill adopt the concepts of "employee" and "officer" that are used in similar provisions of the SFO. If this approach is adopted, we suggest that the Bill adopt the definition of "officer" in Part 1 of Schedule 1 to the SFO, as follows; and

> ***officer*** (高級人員)-
>
> (a) in relation to a corporation, means a director, manager or secretary of, or any other person involved in the management of, the corporation; or
>
> (b) in relation to an unincorporated body, means any member of the governing body of the unincorporated body.

(d) linked to paragraph (c), the meaning of "persons employed in connection with a business" in section 17(2) of the Bill and, in particular, how this differs from the term "persons employed to work for [that business]" currently used in sections 10(7), 10(8), 13(7) and 13(8) of the Bill.

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[27] Paragraph 4.3, Second Consultation Paper.

13 Regulatory sanctions

13.1 We ask that section 21(2)(c) of the Bill be amended so that the pecuniary penalty of *"3 times the amount of the profit gained, or costs avoided, by the financial institution as a result of the contravention"* in subsection (ii) be deleted and that it only contain the specified maximum penalty of $10,000,000 that is currently proposed in subsection (i).

13.2 Our reasons for this request are that:

(a) the penalties proposed in section 21 of the Bill involve strict liability. We suggest that it is not appropriate that an almost unlimited pecuniary penalty apply without a mental threshold;

(b) the "3 times" penalty is uncertain in its operation and could be applied in inconsistent ways by different relevant authorities pursuant to their power to issue guidelines in section 23 of the Bill and their discretion in section 23 generally. We suggest that this distinguishes the Bill from other legislation that has a "3 times" penalty (such as the SFO) and that it is therefore more appropriate that the Bill contain a specified maximum penalty for consistency; and

(c) of the sample FATF member jurisdictions HKAB has reviewed, we understand that only the United States has a similar type of penalty for AML/CTF-related offences, but it requires "intent" or "knowledge".[28]

13.3 HKAB also asks that section 23 of the Bill be enhanced by including the specific matters that should be included in guidelines issued by a relevant authority under that section. For example, we suggest that the matters specified in section 199(2) of the SFO could be adopted, with appropriate adjustments. We would be pleased to discuss this further if required.

14 Individual criminal liability

14.1 We ask that the minimum mental threshold for individual criminal liability under the Bill be an "intent to defraud". That is, we suggest that an individual's potential criminal liability under the Bill should require more than knowledge of a breach - it should require an intention to defeat the purposes of the Bill.

14.2 In particular, we strongly suggest the removal of section 5(7) of the Bill, which imposes criminal sanctions (including possible imprisonment) where *"a person who is an employee of a financial institution or is employed to work for a financial institution or is concerned in the management of a financial institution knowingly causes or knowingly permits the financial institution to contravene the specified provision"*.

14.3 In support of this proposal, HKAB observes that:

(a) FATF Recommendation 17 requires that sanctions deal with contraventions by both natural and legal persons, but in each case, requires them to be "proportionate";

(b) the requirements in Schedule 2 - many of which are "specified provisions" for the purpose of section 5(7) of the Bill - involve the exercise of judgment and discretion. We suggest that this cogent interpretative element distinguishes the Bill from similar liability provisions in other legislation, and that it is not appropriate that an individual face criminal liability for a knowing breach of requirements that are open to reasonable interpretation, without the additional element of intent;

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[28] 18 U.S.C. §1956, (a)(i), Money Laundering Control Act 1986.

(c) the current proposals in section 5(7) apply to a very broad range of persons, who may not necessarily occupy senior positions of responsibility in relation to AML/CTF matters; and

(d) the criminal liability provisions in sections 10 and 13 of the Bill adopt the approach of requiring individuals to have an "intent to defraud";[29] which we suggest is also an appropriate and proportionate approach to liability for Schedule 2-related contraventions.

14.4 If the Administration does not agree with this proposal, HKAB asks that the criminal liability for any offence committed by an individual with the *mens rea* of knowledge only be limited to a maximum pecuniary penalty, to help address these concerns in relation to proportionality.

14.5 Last, we also re-iterate our requests for clarification in paragraph 12.7(c) in relation to the categories of individuals currently specified in sections 5(7) and (8) of the Bill.

Part D - Implementation of the Bill

15 Implementation timing

15.1 HKAB understands the need to implement Hong Kong's statutory AML/CTF framework for the financial sector efficiently and to make every effort to implement the regime by mid-2012 to meet FATF's expectations. We are also aware that the current scheduled implementation date is 1 April 2012, as set out in section 1 of the Bill.

15.2 HKAB also fully endorses the Administration's statement in the Background Brief to the Bills Committee (extracted in paragraph 9.2) that there should be a *"reasonable lead time between the enactment and commencement of the legislation"*. We suggest that the importance of supplementary guidelines to the operation of the Bill also requires a reasonable lead time between the issuance of the final Unified Guideline and Sectoral Guidelines and the commencement of the legislation. HKAB members require this time to finalise a concrete action plan.

15.3 In this regard, we ask that:

(a) the consultation process for the Unified Guideline and Sectoral Guidelines commence as soon as possible. In this regard, we have provided our initial suggestions as to our suggested content of those guidelines in this response (please refer to paragraph 2). HKAB would also be pleased to render such further assistance that is necessary to help expedite this process;

(b) the Bill commence at least 12 months after the Bill, the Unified Guideline and the Sectoral Guidelines are in final form. This is essential to allow financial institutions to implement the policies and procedures, and deploy the resources, necessary to comply with the Bill;

(c) the Bill, the Unified Guideline and the Sectoral Guidelines commence on the same date, to ensure a consistent approach to AML/CTF from the very beginning; and

(d) section 1(4) of the Bill be amended as follows, to clarify that the Bill will not commence before 1 April 2012, which we suggest is important for market certainty and critical for planning.

> (4) The Secretary for Financial Services and the Treasury may, by notice published in the Gazette, amend the date specified in subsection (2) to a later date.

[29] Sections 10(7), 10(8), 13(7) and 13(8), Bill.

15.4 As an ancillary matter, we have assumed, in preparing this response, that the existing HKMA Guideline and Supplement will be replaced with a new Sectoral Guideline (or amended as appropriate) as part of the implementation process for the Bill, so that the requirements form a cohesive set of principles.

16 Public education

16.1 The FSTB has indicated that it will work closely with relevant authorities to *"arrange workshops and training sessions to facilitate [financial institutions] to familiarize with the new requirements. Mass publicity will be arranged to enhance public awareness of the new requirements"*.[30]

16.2 HKAB fully supports this endeavour, and emphasises the need to educate all financial services industry participants, including the general public. In particular, we ask that the FSTB and relevant authorities undertake a coordinated approach to public education before the commencement of the Bill. We also suggest that public education cover the following key areas:

(a) the circumstances in which information may need to be provided;

(b) the types of information that may be required for certain common activities (for example, to open a banking account or to conduct a money transfer overseas);

(c) when an account might be closed, a transaction refused or another business relationship terminated;

(d) the importance of AML/CTF controls; and

(e) where to obtain more information.

17 Future changes

17.1 HKAB and its members dedicate substantial resources to AML/CTF-related issues, including complying with current requirements and responding to changes as they arise. We also have significant collective experience on practical compliance issues. Accordingly, we suggest that future changes to the Bill (including Schedule 2), the Unified Guidelines or the Sectoral Guidelines, once they are implemented, be the subject of public consultation wherever possible, or at the minimum, industry stakeholder consultation.

17.2 We suggest that this consultation is also important because of the serious liabilities imposed under the Bill for compliance failures.

Part E - Ancillary matters

18 Customers who are not physically present for identification purposes

18.1 Consistent with our request in paragraph 10 in relation to the measures that need to be taken in high risk situations, HKAB suggests that section 9 of Schedule 2 is overly prescriptive and may not effectively address the risks of money laundering and terrorist financing in a sufficiently broad range of circumstances. To address this concern, we suggest that:

(a) examples of the measures that can be taken in these circumstances should be shifted into Sectoral Guidelines; and

[30] Paragraph 8.3, Second Consultation Paper.

(b) the obligation be adjusted to reflect paragraph 48 of the Basel "Customer due diligence for banks" paper, so that section 9 of Schedule 2 is revised so that it reads as follows.

> A financial institution must apply equally effective customer identification procedures for customers who are not physically present for identification purposes, on a risk-sensitive basis, as those who are available for physical interview.

18.2 If the concepts used in section 9 of Schedule 2 are retained (either in the Bill or the Sectoral Guidelines), we would be grateful for the following additional clarifications in an appropriate level of non-statutory guidance:

(a) the "appropriate persons" who can certify the relevant documents (eg solicitors and notaries); and

(b) what constitutes a "business similar to that carried on by an authorized institution", and an authority "that performs functions similar to the Monetary Authority".

19 Politically exposed persons

19.1 Consistent with our requests in paragraphs 10 and 18, we ask that section 10 of Schedule 2 to the Bill be adjusted as follows.

> (1) If a financial institution knows, from publicly known information or information in its possession, that a customer or a beneficial owner of a customer is a politically exposed person, it must~~, before establishing a business relationship with the customer,~~ take reasonable measures to mitigate any risk of money laundering and terrorist financing associated with that business relationship, on a risk-sensitive basis. Such measures must be undertaken either—
>
> (a) before establishing a business relationship with the customer; or
>
> (b) as soon as reasonably practicable after establishing a business relationship with the customer, if this is necessary not to interrupt the normal conduct of business with regard to the customer.
>
> ~~(a) obtain approval from its senior management; and~~
>
> ~~(b) take adequate measures to establish the customer's or beneficial owner's source of wealth and the source of the funds that will be involved in the proposed business relationship.~~
>
> (2) If a financial institution comes to know, from publicly known information or information in its possession, that an existing customer or a beneficial owner of an existing customer is a politically exposed person or has become a politically exposed person, it must take reasonable measures, on a risk-sensitive basis, to mitigate any risk of money laundering and terrorist financing associated with that business relationship and must not continue its business relationship with the customer unless it has taken such measures within a reasonable time.~~—~~
>
> ~~(a) has obtained approval from its senior management; and~~
>
> ~~(b) has taken adequate measures to establish the customer's or beneficial owner's source of wealth and the source of the funds that are involved in the business relationship.~~

19.2 We suggest that these adjustments will provide the necessary flexibility to determine a contextually-appropriate course of action and avoid unnecessarily disrupting normal business activities. We believe that it is more appropriate that the Unified Guideline (with

support from Sectoral Guidelines) identify the precise measures that should be taken - and the forms of evidence that would be acceptable - with appropriate alternatives if certain steps are not possible in the circumstances.

19.3 We suggest that this is preferable to a prescriptive approach, where the only alternative is not commencing or terminating a business relationship. In our experience, this is particularly relevant to establishing the customer's source of wealth or funds, which takes time. HKAB also advocates the use the term "reasonable measures" rather than "adequate measures". "Reasonable measures" is the wording used in the corresponding FATF Recommendation 6(c) and section 10.5a of the HKMA Supplement.

19.4 In connection with these adjustments, we also ask that the definition of "politically exposed person" in section 1(1) of Schedule 2 to the Bill be:

(a) adjusted to include a timing cap on persons who may have been politically exposed in the past, consistent with the approach taken in other jurisdictions[31] and bearing in mind that any other circumstances of high risk will need to be addressed in accordance with section 15 of Schedule 2 to the Bill. Specifically, we suggest the following adjustment to paragraph (a) of that definition;

> an individual who is or has, at any time in the preceding year, been entrusted with a prominent public function in a place outside the People's Republic of China …

(b) clarified with a list of persons who are considered to hold a sufficiently prominent public function be issued from time to time, similar to section 4 of schedule 2 to the United Kingdom Money Laundering Regulations (2007) and lists issued by commercial list providers suggested by the Australian AUSTRAC Regulatory Guide[32] from time to time. We suggest that the FSTB may be an appropriate body to undertake this role; and

(c) supplemented with additional non-statutory guidance in the Unified Guidelines:

(i) in relation to assessing whether a post is "senior", "important", "middle-ranking" or "junior", including examples;

(ii) what a "state-owned corporation" is; and

(iii) containing language similar to section 10.4 of the HKMA Supplement, which says that due diligence *"…could be achieved, for example, by screening the name of the customer and connected parties against publicly available information or a commercial electronic database"*.

19.5 We also suggest that the related definition of "close associate" in section 1(3) of Schedule 2 to the Bill be shifted into the Unified Guideline, where we suggest it can be explained more fully. We also wish to clarify whether it might be more appropriate to use the word "or" instead of "and", at the end of subsection (a) of this definition.

19.6 Finally, HKAB wishes to:

(a) clarify that section 10 to the Bill only relates to customers with whom a financial institution has, or proposes to establish, a business relationship. That is, our understanding is that it does not apply to occasional transactions; and

(b) raise the issue of "domestic politically exposed persons", which is the subject of a FATF Consultation Paper released on 26 October 2010. If these proposals are

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31 For example, regulation 14(5), definition of "politically exposed person", Money Laundering Regulations (2007) (United Kingdom).

32 Chapter 4, Part B, AUSTRAC Regulatory Guide, available at www.austrac.gov.au/regulatory_guide.html.

carried forward, we would be pleased to discuss their implementation in Hong Kong with the Administration, the FSTB and the HKMA.

20 Public bodies

20.1 A number of HKAB members have concerns about determining whether or not a person is a "public body" under the definition proposed in section 1(1) of Schedule 2 to the Bill. For example, we wish to clarify whether the following entities would be considered to be "public bodies" (and if so, under which paragraph of the definition):

(a) each "relevant authority" for the purposes of the Bill;

(b) the Office of the Privacy Commissioner for Personal Data;

(c) the Equal Opportunities Commission;

(d) Hong Kong Mortgage Corporation Limited;

(e) MTR Corporation Limited and its subsidiaries;

(f) Hong Kong International Theme Parks Limited;

(g) state-owned enterprises; and

(h) joint ventures with a foreign government at a municipal, provincial or state level.

20.2 To help address these concerns, we suggest that the definition of "public body":

(a) include a new paragraph (f) that states words to the following effect; and

> (f) any person designated by the Secretary for Financial Services and the Treasury as a "public body" for the purposes of this Ordinance, by notice published in the Gazette.

(b) be supported by detailed practical guidance (with examples) in the Unified Guideline.

21 Trusts

21.1 The proposals in the Second Consultation Paper limited the customer due diligence measures to "legal arrangements", which was defined as an express trust or an arrangement with a similar effect.[33] Section 2 of Schedule 2 to the Bill makes no such reference to an express trust concept - it applies to trusts generally.

21.2 To address the problem of identifying the beneficiaries of a discretionary trust, we suggest either that:

(a) section 2(b) of Schedule 2 to the Bill be amended to refer only to an "express trust", which would be consistent with FATF Recommendation 34 and the Second Consultation Paper; or

(b) appropriate provisions (similar to section 11 of Schedule 2 to the Bill) be adopted to deal with this issue.

21.3 HKAB also asks that the Unified Guideline provide detailed guidance on opening trust accounts generally and in relation to performing due diligence on a customer whose chain of ownership includes a trust.

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[33] Proposal 5(b), Second Consultation Paper.

22 Carrying out due diligence via intermediaries

22.1 HKAB welcomes the proposals in section 18 of Schedule 2 to the Bill in relation to carrying out due diligence measures by means of "specified intermediaries". In connection with these proposals, we have a small number of suggestions.

22.2 First, in relation to the professionals that can be "specified intermediaries", we ask that:

(a) professional firms (such as a firm of solicitors or accountants), and not only individual professionals (for example, a lawyer or accountant), be contemplated by this section. We note that the corresponding FATF Recommendation 9 does not specify that the intermediary must be an individual and we suggest that this change will make the arrangements substantially more practicable;

(b) the original proposal in the Second Consultation Paper[34] to include Hong Kong professionals who are subject to, and supervised in relation to, requirements similar to those in Schedule 2 to the Bill (that is, the local equivalent of the specified intermediaries in section 18(3)(c) of Schedule 2) be reinstated. We suggest that this is a very important type of specified intermediary for the financial services industry. It is different than the concept in section 18(3)(a) of Schedule 2 - which only lasts for 3 years[35] - because it has additional strict supervisory and compliance measures; and

(c) the Unified Guideline clarify whether the following would be considered to be specified intermediaries:

(i) the Mandatory Provident Fund Authority (and similar organisations in other countries); and

(ii) self-regulatory organisations (being non-government institutions that regulate the activities of their members).

22.3 HKAB also suggests that the Unified Guideline provide clear guidance as to the meaning of section 18(6) of Schedule 2 to the Bill, and how agency arrangements contemplated by that section should be distinguished from intermediary arrangements under section 18(1).

22.4 We also suggest that this legislative process provides a good opportunity to clarify the following regulatory issues in a Sectoral Guideline for authorised institutions:

(a) how authorised institutions should treat branches of the same legal entity in relation to AML/CTF-related procedural arrangements. In particular, whether these arrangements fall within the purview of section 18(1) and/or section 18(6) of Schedule 2;

(b) whether arrangements with a "specified intermediary" are considered to be "outsourcing" for the purpose of the HKMA's outsourcing guidelines;[36] and

(c) which additional requirements from section 6 of the HKMA Supplement in relation to such arrangements will be carried forward.

23 Branches and subsidiaries

23.1 HKAB understands that the extraterritorial measures proposed in section 22 of Schedule 2 are, in substance, required under FATF Recommendation 22.

23.2 To assist in making these measures as operationally practicable as possible, we ask that:

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34 Proposal 10(e)(ii), Second Consultation Paper.

35 Pursuant to section 18(5) of Schedule 2, Bill.

36 HKMA Supervisory Policy Manual SA-2, Outsourcing.

(a) section 22(1) of Schedule 2 include a concept of "reasonable steps", in recognition that a financial institution may not have comprehensive control of its offshore operations, even though it may direct its policies and protocols;

(b) this requirement be narrowed to refer to *"majority owned subsidiary undertakings"*, which reflects the approach taken in FATF Recommendation 22;

(c) the requirement to take additional measures to mitigate any AML/CTF risks - if local law requirements restrain the application of the specified measures - in section 22(2)(b) of Schedule 2 be removed. This does not appear in FATF Recommendation 22 and imposes potentially very onerous (and unspecified) requirements on financial institutions. As an alternative, we ask that the requirement to take additional measures refer to consultation with the relevant authority; and

(d) section 22(2) of Schedule 2 recognise that even if foreign law permits a procedure, it may not be reasonably practicable or appropriate to apply it.

23.3 Our suggested drafting adjustments to reflect these proposals and our suggestions in paragraph 3 (in relation to benchmarking) are as follows.

> (1) A financial institution incorporated in Hong Kong must take reasonable steps to ensure that—
>
> (a) its branches; and
>
> (b) its majority owned subsidiary undertakings that carry on the same business as the financial institution in a place outside Hong Kong,
>
> have procedures in place to ensure compliance with, subject to subsection (2)~~to the extent permitted by the law of that place~~, requirements broadly equivalent ~~similar~~ to those recommended by the Financial Action Task Force ~~imposed under Parts 2 and 3 of this Schedule~~ that are applicable to the financial institution.
>
> (2) If the law of the place at which a branch or subsidiary undertaking of a financial institution carries on business does not permit the application of any procedures relating to any of the requirements referred to in subsection (1) or it would otherwise be reasonably impracticable or inappropriate to apply them, the financial institution must—
>
> ~~(a)~~ inform the relevant authority accordingly.~~; and~~
>
> ~~(b) take additional measures to effectively mitigate the risk of money laundering and terrorist financing faced by the branch or subsidiary undertaking as a result of its inability to comply with the requirement.~~

23.4 In connection with these measures, HKAB would also be grateful if the Administration could please clarify:

(a) whether a "branch", as defined,[37] is intended only to capture branches of the same legal entity as the financial institution; and

(b) what constitutes a "business similar to that carried on by the financial institution" (in the definition of "branch"). We suggest that this clarification, with examples and criteria, could also be contained in the Unified Guideline.

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[37] Defined in section 22(3) of Schedule 2, Bill.

23.5 We also suggest that section 22 of Schedule 2 also include a specific provision that empowers relevant authorities to issue Sectoral Guidelines to financial institutions in relation to implementing these requirements.

24 Money service operators

24.1 HKAB fully supports the introduction of a licensing regime for RAMCs under Part 5 of the Bill, and the extension of AML/CTF standards to these entities. In particular, we are aware that the implementation of an effective regulatory regime for RAMCs was a key focus of FATF's 2008 mutual evaluation report on Hong Kong.

24.2 Among other things, FATF observed that:

> *"[r]emittance agents and money changers are not routinely monitored or supervised for AML/CFT; and there are no measures to prevent criminals from controlling or managing these businesses".*[38]

24.3 We suggest that the current legislative process provides an excellent opportunity to introduce high standards of conduct that are consistent with those imposed on other types of financial institutions. We believe that this will strengthen Hong Kong's reputation as a leading international financial market and the perceived integrity of the Hong Kong financial services industry as a whole.

24.4 Bearing in mind the concerns raised by FATF and HKAB's interest in a strong financial services market, we suggest that the proposals in Part 5 could be enhanced through:

(a) implementing a Sectoral Guideline in tandem with the commencement of the Bill that:

(i) specifies precise 'fit and proper' criteria for the purpose of section 30(3)(a), based upon the SFC's Fit and Proper Guidelines and the approach taken in jurisdictions such as Singapore.[39] We suggest that this criteria include:

(A) a minimum age of 18 years;

(B) minimum education, qualification and experience requirements;

(C) meeting competence requirements (including never having evidenced incompetence, negligence or mismanagement); and

(D) sound financial condition and history; and

(E) all necessary infrastructure, training and controls. We suggest that simple domestic operations that simply use internet banking to facilitate remittance transactions are inappropriate; and

(ii) explains the types of premises that are "suitable" for the purposes of section 30(3)(b), which we suggest include stringent and objective criteria. For example, the criteria could include the requirement to demonstrate that the premises have the infrastructure to:

(A) conduct the business;

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38 Page 12, Summary of the Third Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism, Hong Kong China", 20 June 2008.

39 The requirements are contained in sections 5 and 6 of the Singapore Money-Changing and Remittance Businesses Act (Cap. 187).

(B) manage risk effectively; and

(C) provide a proper audit trail,

similar to the guidance provided in section 6.1.2(b) the SFC's Fit and Proper Guidelines;

(b) adjusting section 30(3)(c) to require that any domestic use of the premises must not affect the exercise of any supervisory powers under the Bill, similar to section 130 of the SFO, which concerns the approval of premises for record-keeping purposes;

(c) adding to section 30(3) of a requirement that the applicant have its business registered under the Business Registration Ordinance (Cap. 310). We suggest that this would add an additional layer of regulatory oversight and be consistent with the definitions of "money changing service" and "remittance service" in Part 1 of Schedule 1 the Bill, which contemplate the provision of a service and the carrying on of a business, respectively; and

(d) including a conviction under section 24B or 24C of the Organized and Serious Crimes Ordinance (Cap. 455) in section 30(4)(a)(iv) as one of the factors in determining whether or not a person is "fit and proper". Although these provisions are proposed to be repealed pursuant to section 86 of the Bill, we suggest that a past conviction would still be relevant.

24.5 HKAB also has the following supplementary suggestions:

(a) First, we suggest that in the interests of a streamlined legislative approach, the Money Changers Ordinance (Cap. 34) either be:

(i) repealed, with relevant provisions consolidated into the AML Ordinance; or

(ii) adjusted so that the relevant provisions (in particular, the exemptions) be aligned with the AML Ordinance.

(b) Second, we suggest that the exemptions from Part 5 of the Bill for financial institutions other than authorised institutions:[40]

(i) be aligned with the exemption from the money broker requirements in the Banking Ordinance,[41] to maximise drafting consistency across regimes. We suggest that each exemption read as follows.

> a [name of financial institution] that operates a money service that is ancillary or incidental to a business carried on by that person which, if the business is, or were to be, carried on in or from Hong Kong, is not, or would not be, as the case may be, the business of operating a money service

(ii) be accompanied by interpretative guidance in the Unified Guideline on the meaning of "ancillary" (and if adopted, "incidental") and examples of the types of money services that would be excluded, similar to the guidance helpfully provided by the HKMA in relation to the money brokerage provisions.[42] HKAB suggests that this guidance is

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40 Sections 25(b) to (e), Bill.

41 Paragraph (b)(i) of the definition of "money broker", section 2(1) of the Banking Ordinance. However, we have left out the word "wholly" (as in "wholly ancillary or incidental") which is used in section 2 of the Banking Ordinance, because there is no common law meaning for this.

42 Paragraph 11.8 of the HKMA's "Guide to Authorization", available online at www.info.gov.hk/hkma.

particularly important for foreign currency spot transactions, which fall under "money changing services".

(c) Third, in relation to the secrecy provisions in section 48, we ask that:

(i) any foreign bodies to whom the Commissioner can disclose information under section 48(3)(d) of the Bill be required to be published in the Gazette. We suggest that this is important to enhance transparency and allow financial institutions to understand how information that they may be compelled to disclose to the Commissioner may be used; and

(ii) as per the SFO, there be a mandatory condition on non-disclosure imposed on anyone who may receive information from the Commissioner, rather than this being discretionary (as currently proposed in section 48(6) of the Bill).

(d) Last, we would be grateful for the Administration to confirm that the register of money service operators required to be maintained under section 27 of the Bill will be publicly available electronically. HKAB suggests that this is important for the transparency of the money services industry. We also ask that section 27 be adjusted to allow financial institutions to apply in writing to the Commissioner for additional information about money service operators (including identification numbers) that may not be accessible on the register, for verification purposes.

25 Record-keeping

25.1 Several HKAB members have expressed serious concerns about the requirement proposed in section 20 of Schedule 2 to the Bill to keep all business correspondence for the periods specified in that section. In particular, members are concerned that this will pose an unreasonable administrative burden - for example, the requirement would ostensibly extend to every email exchanged between a relationship manager and their customer.

25.2 We suggest that this requirement either be deleted or that the correspondence that is required to be kept be restricted to specific types of correspondence that are specified in Sectoral Guidelines.

25.3 As an ancillary point, we suggest that the requirement in section 20(6) in relation to intermediaries be shifted into section 18 of Schedule 2 so that a financial institution's obligations relating to intermediaries are grouped thematically and easy to locate.

26 Secrecy

26.1 We suggest that the Administration take the opportunity presented by this legislative review process to harmonise (and in some cases, strengthen) the secrecy provisions across the regulatory regimes applicable to the financial institutions covered by the Bill. We suggest that this is important because of relevant authorities' broad rights of inspection and investigations under this Bill, which can extend to entities that they do not primarily regulate.

27 Additional clarifications and suggestions

27.1 HKAB suggests that section 59, which relates to appeals to the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Review Tribunal ("**Tribunal**"), include a qualitative requirement that an appeal be heard by the Tribunal "as soon as reasonably practicable". HKAB recognises the difficulty of imposing a specific time frame, but we suggest that it is important that an administrative review on AML/CTF-related issues, which can involve highly sensitive matters, be conducted expeditiously.

27.2 Some HKAB members have expressed a concern about:

(a) the possibility of inadvertently disclosing customer information in connection with an appeal to the Tribunal and the information-gathering powers of the Tribunal in section 60 of the Bill. While we recognise (and support) the privilege against disclosure offered by section 63, we would be grateful if the Administration could please confirm that if the subject of an appeal is unclear, an authorised institution may request further information to enable it to assess its rights under section 63; and

(b) the circumstances in which the Tribunal will hold a private hearing. To provide certainty, we ask that subsidiary rules specify the factors that will be taken into account by the Tribunal when determining whether or not a hearing should be held in private, pursuant to its powers in section 6(7) of Schedule 4 to the Bill.

27.3 Linked with our comments in paragraph 12.7(c), HKAB wishes to understand the difference between "employee" and "staff member" in section 78 of the Bill. While section 78 is otherwise consistent with section 388 of the SFO, the latter term ("staff member") does not appear in that section.

27.4 We recommend that the notice provisions in section 79 of the Bill be adjusted to include a reference to notices to be given to the Postmaster General. We suggest that the reference could be added either to the existing section 79(1) or a new subsection.

27.5 HKAB suggests that the proposed amendment of section 180 of the SFO in section 87 of the Bill is unnecessary in light of the broad scope of the inspection provisions proposed in section 9 of the Bill.

27.6 We suggest that section 17(2) of Schedule 2, which describes when a corporation has a "physical presence" in a particular place, should apply to both instances in which that reference appears - that is, subsection (1)(c) (as currently drafted) and subsection (1)(d)(iiii), as follows.

> (2) For the purposes of subsections (1)(c) and (1)(d)(ii), a corporation has a physical presence in a place if—
>
> (a) the corporation carries on banking business at any premises in that place; and
>
> (b) at least one full-time employee of the corporation performs banking-related duties at those premises.

Annexure 1 - Risk-based approach

This schedule contains HKAB's suggested drafting adjustments to Schedule 2 to the Bill, in connection with our comments in relation to the need for risk-based approach in paragraph 1 of our response. We emphasise that these adjustments are based on the current text of the Bill and are not intended to undermine any comments we have made in the main body of our response.

1 Section 2 of Schedule 2

The following measures are customer due diligence measures applicable to a financial institution, which may be carried out on a risk-sensitive basis—

2 Sections 4(1) and (3) of Schedule 2

… a financial institution may… carry out only the measures set out in section 2(a), (c) and (d) of this Schedule, on a risk-sensitive basis, in relation to a customer…

3 Section 5(1) of Schedule 2

A financial institution must continuously monitor its business relationship with a customer, on a risk-sensitive basis, by—

4 Section 5(3) of Schedule 2

…the financial institution must, in monitoring its business relationship with the customer under this section, take additional measures, on a risk-sensitive basis, to compensate for any risk of money laundering…

5 Section 6(1) of Schedule 2

"…a financial institution must… carry out the customer due diligence measures on a risk-sensitive basis when-"

6 Section 9 of Schedule 2 *

If a customer has not been physically present for identification purposes, a financial institution must carry out at least one of the following measures, on a risk-sensitive basis—

* Please refer to HKAB's preferred language in paragraph 18.1 of our response.

7 Sections 10(1)(b) and (2)(b) of Schedule 2

Please refer to our suggested language in paragraph 19.1 of our response.

8 Section 11(2) of Schedule 2

(2) A financial institution must carry out the measures specified in subsection (3), on a risk-sensitive basis—

9 Section 14(1) of Schedule 2

(1) An authorized institution must, before establishing a correspondent banking relationship with an institution located in a place outside Hong Kong… authorized institution, on a risk-sensitive basis—

10 Section 15 of Schedule 2

Please refer to our suggested language in paragraph 10.1 of our response.

Annexure 2 - Non-statutory guidelines

This schedule contains the key matters that HKAB suggests should be included in non-statutory guidelines and our suggested changes to section 7 of the Bill. It relates to our comments in paragraph 2 of our response and also includes the suggestions we have raised elsewhere in our response in relation to specific matters.[43]

1 Requested areas of guidance

Bill ref.	Guidance requested by HKAB	Suggested guideline	
		Unified	Sectoral
Matters that affect a range of provisions			
-	Qualitative guidance and examples of the types of persons who should be treated as "customers", particularly in the context of overseas accounts and transactions.	√	
-	Examples of the types of evidence that are acceptable to meet the customer due diligence requirements in a range of practical circumstances, similar to the guideline produced by the Joint Money Laundering Steering Committee in the United Kingdom. For example, guidance on: ▪ the methods of verifying a person's source of wealth and source of funds; ▪ what is considered to be a "reliable and independent source", for the purposes of section 2(a)(iv) of Schedule 2; ▪ when a person's address needs to be verified;[44] ▪ confirmation that only two signatories on an account need to be verified;[45] ▪ whether sole proprietorships may use their business registration certificate as evidence.	√	√ *Supplementary*
-	When self-certification of particular matters would be acceptable. For example, director declarations regarding a corporation's ongoing registration and structure, or declarations by a trustee where the trust deed is not available.	√	√ *Supplementary*
-	The meaning of "ultimate control" (with examples) for the purpose of the various provisions in which it appears.	√	
-	Suspicious transaction reporting and associated protections from liability, to reflect FATF Recommendations 13 and 14 and the HKMA Supplement.[46] We suggest that such guidance will also be helpful to avoid "tipping off".	√	
-	Criteria to assist in conducting the comparative assessments required under the Bill. For example, to	√	

[43] Paragraphs 11.4 and 11.5 of our response also contain matters that HKAB suggests should be covered in non-statutory guidance, but those suggested matters are only relevant if the Administration does not adopt HKAB's requested approach in relation to the proposals in sections 19 and 23 of Schedule 2 to the Bill (in paragraphs 11.3 and 11.5).

[44] In this regard, we suggest that the guidance mirror paragraph 17 of the Interpretative Notes to the HKMA Supplement, with examples.

[45] Akin to paragraph 19 of the Interpretative Notes to the HKMA Supplement.

[46] For example, paragraphs 3.7, 15.14 and 16.4, HKMA Supplement.

Bill ref.	Guidance requested by HKAB	Suggested guideline	
		Unified	Sectoral
	assist in assessing whether: ▪ an offshore authority is "similar to" a particular domestic authority (eg section 14(1)(b) of Schedule 2); ▪ a person conducts a business "similar to" a particular financial institution (eg section 18(3)(c) of Schedule 2); ▪ particular procedures and measures adopted by a person are "similar" (or, as we have suggested, "broadly equivalent") to the benchmark ultimately selected for the Bill. The guidance should also describe the types of deviations that would be acceptable.		
-	Detailed guidance on opening trust accounts generally and in relation to performing due diligence on a customer whose chain of ownership includes a trust.	√	
-	Protocols in relation to refusing a transaction, closing an account and otherwise terminating a business relationship. We suggest that these protocols link with the guidelines on suspicious transaction reporting and include an option for financial institutions to obtain the relevant authority's consent to take such action in relation to a customer.		√
-	Guidance on the interaction of the AML/CTF due diligence requirements and Hong Kong's privacy standards.	√	
Matters relating to specific provisions of Schedule 2 to the Bill			
1	Who is the "beneficial owner", or has "ultimate control", of a corporation, trust and partnership and, in each case: ▪ how the beneficial owner / ultimate controller should be determine and verified; and ▪ what alternative measures can be taken if this is not practicable in the circumstances.	√	
	In relation to the beneficial owner of a corporation specifically, HKAB asks that: ▪ the beneficial ownership of a corporation be determined only by reference to voting rights[47] and not also to the general ownership / control of its issued share capital.[48] This is consistent with the current reference point under the HKMA Supplement.[49] We also suggest that voting control is the most appropriate test because it: o relates to the shareholders of a corporation who have operative control of it; and o is a clearer and more practicable test than a general test of owning or controlling the issued share capital of a corporation, which can be difficult to determine in practice;	√	

[47] Currently proposed in section 1(1) of Schedule 2 to the Bill (paragraph (a)(ii) of the definition of "beneficial owner").

[48] Currently proposed in section 1(1) of Schedule 2 to the Bill (paragraph (a)(i) of the definition of "beneficial owner").

[49] Paragraph 13, Interpretative Notes to the HKMA Supplement.

Bill ref.	Guidance requested by HKAB	Suggested guideline	
		Unified	Sectoral
	▪ the Administration please clarify if paragraph (ii) of the definition of the beneficial owner of a corporation (relating to voting control) is also intended to extend to voting right entitlements obtained "through a trust or bearer share holding" (as per paragraph (i)); and ▪ if the general test of owning or controlling the issued share capital of a corporation is retained (contrary to our request), that "issued share capital" be defined or explained so that it is clear whether or not it includes preferential shares that have been issued by the corporation.		
	How financial institutions can determine, and conduct due diligence on, the beneficial owner(s) of a customer who fall(s) within the 'catch-all' paragraph (d) of the definition of "beneficial owner", where the customer is an entity with beneficiary/ies yet to be determined.	√	
	What constitutes a "business relationship" as opposed to an "occasional transaction". In particular, the meaning of "an element of duration".	√	
	Detailed practical guidance (with examples) that explains the concept of "public body".	√	
	A list of jurisdictions that are considered to meet the requirements of the definition of "equivalent jurisdiction", with additional criteria to assist financial institutions to assess other jurisdictions (with guidance on the types of deviations that are acceptable).	√	
1(1),[50] 2(a)(i), 2(d)(i)(A), 11(3)(a)(i) and 12(4)(a)	The meaning of "governmental body" (with examples of the types of bodies that would fall within this concept), including a clarification as to whether the Administration intends the word "governmental" to be interpreted only as the Hong Kong government and how this concept overlaps with the concept of "public body".	√	
3(1)(b)	Detailed practical guidance on the due diligence requirements for "linked" transactions. For example, how long monitoring needs to be undertaken and the different requirements required for lower or higher risk situations.	√	√ *Supplementary*
3(2)	Qualitative guidance on, and examples of, the circumstances in which carrying out due diligence measures after establishing a business relationship would be acceptable.	√	√ *Supplementary*
3(3)	Qualitative guidance on the meaning of "as soon as reasonably practicable", with non-binding examples of periods that a relevant authority would consider acceptable in particular types of circumstances.		√
5	Suggested trigger events to describe the "appropriate times" that due diligence should be conducted after a customer is onboarded (see our comments in paragraph 8) and additional guidance explaining: ▪ transactions that are "complex, unusually large in amount or of an unusual pattern" and which have "no	√	

[50] Paragraph (f) of the definition of "identification document".

Bill ref.	Guidance requested by HKAB	Suggested guideline	
		Unified	Sectoral
	apparent economic or lawful purpose" for the purpose of section 5(1)(c) of Schedule 2 to the Bill, including examples that are relevant to different types of institutions and cover a range of domestic and offshore circumstances; ▪ when a "material change occurs in the way in which the customer's account is operated" for the purpose of the trigger event currently proposed in section 6(1)(c) of Schedule 2; ▪ what will constitute sufficient "additional measures" for the purpose of section 5(3) of Schedule 2 to the Bill; ▪ the precise types of information that should be re-reviewed and when this should be done; and ▪ that a requirement to conduct ongoing due diligence when documentation standards change (currently proposed in section 6(1)(b) of Schedule 2) only applies to a customer in relation to whom an institution has already conducted due diligence under the new regime.		
9	Examples of the measures that can be taken where a person is not physically present for identification purposes.		√
9(b)	The "appropriate persons" who can certify the relevant documents (eg solicitors and notaries).		√ *(or the Bill)*
9(c)(2) (B) and (D)	What constitutes a "business similar to that carried on by an authorized institution", and an authority "that performs functions similar to the Monetary Authority".		√
10	The measures that should be taken in relation to politically exposed persons - and the forms of evidence that would be acceptable - with appropriate alternatives if certain steps are not possible in the circumstances. (Please also refer to our comments in paragraph 19 in relation to this request.)	√	√ *Supplementary*
	Practical guidance: ▪ in relation to assessing whether a post is "senior", "important", "middle-ranking" or "junior", including examples; ▪ what a "state-owned corporation" is; and ▪ containing language similar to section 10.4 of the HKMA Supplement, which says that due diligence *"…could be achieved, for example, by screening the name of the customer and connected parties against publicly available information or a commercial electronic database"*.	√	
	The definition of "close associate" (currently in section 1(3) of Schedule 2 to the Bill) with additional qualitative guidance to assess whether a person falls within this definition.	√	
12	Clarification that a financial institution is not required to enquire as to whether or not a wire transfer represents a batch file.	√	
12(6) and (9)	If the proposed requirements on beneficiary institutions are retained, practical step-by-step guidance on the practical implementation of the information-gathering requirements.	√	

Bill ref.	Guidance requested by HKAB	Suggested guideline	
		Unified	Sectoral
14	Examples of correspondent banking.		√
	The meaning of "banking services" within the definition of "correspondent banking" in section 1(1) of Schedule 2. For example, we suggest a definition similar to Australian subsidiary legislation, which defines this as "all banking services that do not involve nostro or vostro accounts",[51] with additional guidance that states that: *"…it is commonly held that:* *a nostro (Latin for 'ours') account is an account a financial institution holds with a foreign financial institution, usually in the currency of the foreign country;* *vostro (Latin for 'yours') account is the account a financial institution holds on behalf of a foreign financial institution."*[52]		√
	The requirement that an authorised institution have "documented its responsibilities and the responsibilities of the proposed respondent bank" (currently in paragraph 14(2)(c) of Schedule 2), bearing in mind the current industry approach on assessing and recording the parties' respective responsibilities (please refer to our comments in paragraph 9.3(a)).		√
	Guidance on correspondent banking generally, including suggested standards and guidance on managing related risks. In particular, HKAB would appreciate non-statutory guidance on: ▪ the sort of evidence that an authorised institution can rely upon in relation to a proposed respondent bank (for example, a certificate, or public records that show that it is incorporated or established in an equivalent jurisdiction); ▪ the methods of assessing a proposed respondent bank's AML/CTF controls and whether an authority has "functions similar to those of the [HKMA]"; and ▪ the types of accounts that are contemplated by section 14(2) of Schedule 2, which are directly operable by a customer.		√
15	Examples of high risk situations and customers and the due diligence measures that should be adopted in relation to them.	√	√ *Supplementary*
18(3)	Practical guidance on determining whether a person falls within the definition of "specified intermediary" - for example, whether the following would be considered to be specified intermediaries: ▪ the Mandatory Provident Fund Authority (and similar organisations in other countries); and ▪ self-regulatory organisations (being non-government institutions that regulate the activities of their members).	√	
18(3)(c)	The meaning of "trust or company service provider".[53]	√	

[51] Section 3.2.2, Anti-Money Laundering and Counter-Terrorism Financing Rules Instrument 2007 (No. 1).

[52] Page 73, AUSTRAC Regulatory Guide 2009.

Bill ref.	Guidance requested by HKAB	Suggested guideline	
		Unified	Sectoral
18(6)	Clear guidance as to the meaning of section 18(6) of Schedule 2 to the Bill, and how agency arrangements contemplated by that section should be distinguished from intermediary arrangements under section 18(1).	√	
18	Additional clarification of the following regulatory issues for authorised institutions: ▪ how authorised institutions should treat branches of the same legal entity in relation to AML/CTF-related procedural arrangements. In particular, whether these arrangements fall within the purview of section 18(1) and/or section 18(6) of Schedule 2; ▪ whether arrangements with a "specified intermediary" are considered to be "outsourcing" for the purpose of the HKMA's outsourcing guidelines; and ▪ which additional requirements from section 6 of the HKMA Supplement in relation to such arrangements will be carried forward.		√
20	The specific types of correspondence that are required to be kept by a financial institution.		√
22	Practical guidance to assist financial institutions to implement the requirements relating to their offshore branches and subsidiaries.		√
22(3)	Interpretative guidance explaining: ▪ whether a "branch" is intended only to capture branches of the same legal entity as the financial institution; and ▪ what constitutes a "business similar to that carried on by the financial institution" (in the definition of "branch"), with specific examples.	√	
Matters relating to other provisions of the Bill			
Part 5 - s25	Interpretative guidance on the meaning of "ancillary" (and if adopted, "incidental") and examples of the types of money services that would be excluded, similar to the guidance provided by the HKMA in relation to the money brokerage provisions in the Banking Ordinance.[54]	√	
Part 5 - s30(3)	Specific guidance in relation to meeting the "fit and proper" criteria for money service operators and ensuring premises are suitable for the purpose of money services. (Please refer to HKAB's specific suggestions in paragraph 24.4.)		√

2 Suggested changes to section 7 of the Bill

(1) A relevant authority or the Secretary for Financial Services and the Treasury may publish in the Gazette any guideline that it considers appropriate for providing guidance in relation to the operation of any provision of Schedule 2. To the extent reasonably practicable, the relevant authority or the Secretary for Financial Services and the Treasury (as the case may be) must consult with relevant stakeholders before publishing any such guideline.

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53 For example, we suggest that this follow the guidance provided in the Glossary to the FATF Recommendations, although we note that FATF uses the term "trust and company service provider".

54 Paragraph 11.8 of the HKMA's "Guide to Authorization", available online at www.info.gov.hk/hkma.

(2) A guideline published by the Monetary Authority, Securities and Futures Commission or Insurance Authority may incorporate or refer to a guideline or document, or any part of a guideline or document, from time to time issued or published by the Monetary Authority, Securities and Futures Commission or Insurance Authority under the relevant Ordinance.

(3) A relevant authority or the Secretary for Financial Services and the Treasury may from time to time amend the whole or any part of any guideline published under this section in a manner consistent with the power to publish the guideline under this section, and—

Annexure 3 - Benchmark adjustments

This schedule contains HKAB's suggested drafting in connection with our comments in paragraph 3 of our response.

1 Section 1(1) of Schedule 2

equivalent jurisdiction *(對等司法管轄區) means—*

…

(b) a jurisdiction that imposes requirements broadly equivalent ~~similar~~ to those recommended by the Financial Action Task Force ~~imposed under this Schedule~~;

2 Sections 4(2)(b)(iii), (d)(ii)(B) and (d)(iii)(C) of Schedule 2

…has measures in place to ensure compliance with requirements broadly equivalent ~~similar~~ to those recommended by the Financial Action Task Force ~~imposed under this Schedule~~;

3 Section 7(2)(c)(i) of Schedule 2

…had verified the identities of those customers, and would continuously monitor its business relationships with those customers, in accordance with requirements broadly equivalent ~~similar~~ to those recommended by the Financial Action Task Force ~~imposed under this Schedule~~;

4 Section 7(2)(c)(ii) of Schedule 2

…was able to provide to it, on request, the documents, data or information obtained by the respondent bank…in accordance with requirements *broadly equivalent ~~similar~~ to those recommended by the Financial Action Task Force ~~imposed under this Schedule~~;*

5 Section 9(2)(c)(ii)(C) of Schedule 2

…has measures in place to ensure compliance with requirements broadly equivalent ~~similar~~ to those recommended by the Financial Action Task Force ~~imposed under this Schedule~~;

6 Section 14(d)(i) and (ii) of Schedule 2

(i) will verify the identities of those customers, and will continuously monitor its business relationships with those customers, in accordance with requirements broadly equivalent ~~similar~~ to those recommended by the Financial Action Task Force ~~imposed under this Schedule~~; and

(ii) will be able to provide to it, on request, the documents, data or information obtained by the proposed respondent bank in relation to those customers in accordance with requirements broadly equivalent ~~similar~~ to those recommended by the Financial Action Task Force ~~imposed under this Schedule~~.

7 Section 18(3)(c)(ii) of Schedule 2

…has measures in place to ensure compliance with requirements broadly equivalent ~~similar~~ to those recommended by the Financial Action Task Force ~~imposed under this Schedule~~; and

8 Section 21 of Schedule 2

Please refer to our suggested language in paragraph 23.3 of our response.

Annexure 4 - Money transfers

This schedule contains HKAB's suggested drafting in connection with our comments in paragraph 7 of our response.

1 General due diligence requirements - section 3(1)(c) of Schedule 2

(1) Subject to section 4 of this Schedule, a financial institution must carry out customer due diligence measures in relation to a customer in the following circumstances—

…..

(c) despite paragraph (b), before carrying out for the customer an occasional transaction that is a money ~~wire~~ transfer involving an amount equal to or above $8,000 or an equivalent amount in any other currency, whether the transaction is carried out in a single operation or in several operations that appear to the financial institution to be linked;

2 Special monitoring requirements - section 12 of Schedule 2

(1) Subject to subsection (2), this section applies to a money ~~wire~~ transfer involving an amount equal to or above $8,000 or an equivalent amount in any other currency, that is carried out by a financial institution.

(2) This section does not apply to the following money ~~wire~~ transfers—

(a) a money ~~wire~~ transfer between two financial institutions if each of them acts on its own behalf;

(b) a money ~~wire~~ transfer between a financial institution and a foreign institution if each of them acts on its own behalf;

(c) a money ~~wire~~ transfer if—

(i) it arises from a transaction that is carried out using a credit card or debit card (such as withdrawing money from a bank account through an automated teller machine with a debit card, obtaining a cash advance on a credit card, or paying for goods or services with a credit or debit card), except when the card is used to effect a transfer of money; and

(ii) the credit card or debit card number is included in the message or payment form accompanying the transfer.

*(3) Before carrying out a money ~~wire~~ transfer, a financial institution that carries out the money transfer (referred to in this Schedule as the ~~is an~~ **ordering institution**) must record—*

(a) the originator's name;

(b) the number of the originator's account maintained with the financial institution and from which the money for the money ~~wire~~ transfer is paid or, in the absence of such an account, a unique reference number assigned to the money ~~wire~~ transfer by the financial institution; and

(c) the originator's address or, in the absence of an address, the originator's customer identification number or identification document number or—~~,~~

(i) if the originator is an individual, the originator's date and place of birth; or

(ii) if the originator is a corporation, the originator's date and place of incorporation or establishment.

(4) The information mentioned in subsection (3)(a) and (c) must, before it is recorded, be verified by the financial institution on the basis of documents, data or information provided by—

(a) a governmental body;

(b) the relevant authority or any other relevant authority;

(c) an authority in a place outside Hong Kong that performs functions similar to those of the relevant authority or any other relevant authority; or

(d) any other reliable and independent source that is recognized by the relevant authority.

(5) Subject to subsections (6) and (7), a financial institution that is an ordering institution must include in the message or payment form accompanying the money ~~wire~~ transfer the information recorded under subsection (3) in relation to the transfer.

(6) A financial institution may, in relation to a domestic money ~~wire~~ transfer, include in the message or payment form accompanying the transfer only the information recorded under subsection (3)(b) in relation to the transfer but if it does so, it must, on the request of the financial institution to which it passes on the transfer instruction or the relevant authority, provide to that financial institution or the relevant authority the information recorded under subsection (3)(a) and (c) in relation to the transfer within 3 business days after it receives the request.

(7) If more than one individual money ~~wire~~ transfer from a single originator is bundled in a batch file for transmission to a recipient or recipients in a place outside Hong Kong, a financial institution is not required to comply with subsection (5) in relation to each of the money ~~wire~~ transfers if—

(a) the information recorded under subsection (3)(b) is included in the message or payment form accompanying each transfer; and

(b) the batch file contains the information recorded under subsection (3).

(8) If a financial institution acts as an intermediate institution that participates in the completion of a money transfer (referred to in this Schedule as an ***intermediary institution****) ~~in a wire transfer~~, it must transmit all of the information that it receives with the transfer to the institution to which it passes on the transfer instruction.*

(9) If a financial institution is the institution at which the money transfer is made available to a person (referred to in this Schedule as the ~~is a~~ ***beneficiary institution****) in a domestic money ~~wire~~ transfer, it should monitor for money transfer messages or payment forms that are not accompanied by the information required under this section. This monitoring may be undertaken on a risk-sensitive basis and, if necessary, conducted after receiving the money transfer. ~~and the wire transfer is not accompanied by the information required under subsection (3)(b), it must—~~*

~~(a) obtain the information from the institution from which it receives the transfer instruction; and~~

~~(b) if the information cannot be obtained, decide whether to refuse to accept the wire transfer having regard to the risk of money laundering or terrorist financing involved.~~

~~(10) If a financial institution is a beneficiary institution in a wire transfer that is not a domestic wire transfer and the wire transfer is not accompanied by all of the information required under subsection (3), it must—~~

~~(a) obtain the missing information from the institution from which it receives the transfer instruction; and (b) if the missing information cannot be obtained, decide whether to refuse to accept the wire transfer having regard to the risk of money laundering or terrorist financing involved.~~

(11) In this section—

business day *(營業日) means any day other than—*

(a) a Saturday, Sunday or a public holiday in Hong Kong; or

(b) a gale warning day or a black rainstorm warning day as defined by section 71(2) of the Interpretation and General Clauses Ordinance (Cap. 1);

domestic wire transfer *(本地電傳轉賬) means a money ~~wire~~ transfer in which the ordering institution and the beneficiary institution and, if one or more intermediary institutions are involved in the transfer, the intermediary institution or all the intermediary institutions are financial institutions located in Hong Kong;*

foreign institution *(外地機構) means an institution—*

(a) that is located in a place outside Hong Kong; and

(b) that carries on a business similar to that carried on by a financial institution;

originator *(匯款人), in relation to a money ~~wire~~ transfer, means—*

(a) the person from whose account with the ordering institution the money for the money ~~wire~~ transfer is paid; or

(b) in the absence of such an account, the person who instructs the ordering institution to carry out the money ~~wire~~ transfer.

Annexure 5 - Ongoing due diligence

This schedule contains HKAB's suggested drafting amendments to section 5 of Schedule 2 to the Bill, in connection with our comments in paragraph 8 of our response.

(1) A financial institution must continuously monitor its business relationship with a customer, on a risk-sensitive basis, by—

(a) reviewing, ~~from time to time~~ at appropriate times notified by a relevant authority in writing, documents, data and information relating to the customer that have been obtained by the financial institution ~~for the purpose of complying with the requirements imposed under this Part~~ to ensure that they are up-to-date, ~~and~~ relevant and comply with the requirements imposed under this Part;

(b) conducting appropriate scrutiny of transactions carried out for the customer to ensure that they are consistent with the financial institution's knowledge of the customer and the customer's business and risk profile, and with its knowledge of the source of the customer's funds; and

(c) identifying transactions that—

(i) are complex, unusually large in amount or of an unusual pattern; and

(ii) have no apparent economic or lawful purpose, and examining the background and purposes of those transactions and setting out its findings in writing.

(2) When a financial institution carries out its duty under subsection (1)(a) in relation to a pre-existing customer before it first carries out the customer due diligence measures in relation to the customer in accordance with the requirements under this Part, the financial institution is only required to review the documents, data and information relating to the customer that are held by it at the time it conducts the review.

(3) If—

~~(a) a customer of a financial institution has not been physically present for identification purposes;~~

(~~b~~a) a customer, or a beneficial owner of a customer, of a financial institution is known to the financial institution, from publicly known information or information in its possession, to be a politically exposed person; or

(~~c~~b) a customer, or a beneficial owner of a customer, of a financial institution is involved in a situation referred to in section 15 of this Schedule,

the financial institution must, in monitoring its business relationship with the customer under this section, take reasonable additional measures, on a risk-sensitive basis, to compensate for any risk of money laundering or terrorist financing that may be caused by the fact that the customer or beneficial owner is a customer or beneficial owner falling within paragraph (a)~~,~~ or (b) ~~or (c)~~.