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Financial Services & the Treasury Bureau
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Attention: Division 7

By Email: aml_consultation@fstb.gov.hk & by post

Dear Sirs,

Legislative Proposal to Enhance the Anti-Money Laundering ("AML") Regime

Further to our submission on 8 October 2009, we write to give our comments in the second round consultation on the proposed new legislation for customer due diligence ("CCD") and record-keeping requirements for Financial Institutions ("FIs") and the regulation of remittance agents and money changers.

Before going into our specific comments, we would like to take this opportunity to express our appreciation to the government for the incorporation of a number of points we raised during the first round consultation on the proposed legislation.

1. General Comments

1.1. General Exemption for MPF / ORSO Schemes

Some of our members who are MPF / ORSO trustees have indicated that MPF and ORSO schemes should be completely exempted from the AML requirements. In other words, they are of the view that even simplified due diligence requirements should not apply to MPF or ORSO schemes at all, given the nature of such schemes.

They would, accordingly, also like to see the definition of “customer” being changed to exclude members of a pension scheme for CDD purposes. These trustees strongly believe that the pension fund business should be treated differently.

1.2. ***Regulatory Approach***

We are concerned with the issue of consistency in the regulatory approach given the different regulators catering to different sectors of FIs. We note that the government proposal to issue a “standard” set of AML guidelines that may be supplemented by sector-specific guidelines issued by the different sector regulators.

Our concern, as highlighted in our first round comments is that some trust and company service providers, given their existing businesses are currently already regulated by one of more regulators. (e.g. HKMA, SFC or MPFA). We believe that service providers who are already subject to an existing regulatory regime in respect of AML should not be subjected to an additional or parallel regime - i.e. these new proposals should apply only to trust and company service providers not already subject to the AML requirements of the HKMA, SFC or MPFA.

In addition it is necessary that there be consistency, in not only compliance requirements, but also in enforcement standards as well.

1.3. ***Overseas Branches and Subsidiaries***

While Hong Kong-based parent FIs may seek to standardize equivalent measures of CDD and record keeping standards in their overseas branches and subsidiaries, they should not be accountable under the new legislation for a failure to do so if the standards of CDD and record keeping required under the legislation for Hong Kong-based FIs are complied with in Hong Kong.

1.4. ***Powers of the regulatory authorities***

The proposed new legislation will confer powers to the regulatory authorities to supervise financial institutions’ compliance with the statutory requirements. For the purpose of exercising their functions under the new legislation, AML regulatory authorities will be empowered to access and make copies of or extract from books/records and other relevant information maintained by financial institutions for inspection and examination. Whilst it is important for the regulators to have the power for inspections under the new legislation, the power should be exclusive to CDD books and records only.

1.5. ***Criminal Liability***

Taking into account comments received in the first-round consultation, the proposed legislation provides that only those persons who knowingly contravene the statutory obligations will attract criminal liability. If the offence is committed with intent to defraud, a more severe level of criminal sanction will be imposed. We consider that the new legislation needs to reflect the scope of these concepts (e.g. “knowingly contravene”, “intend to defraud”) in the specific context of AML systems and controls.

1.6. ***Others***

The existing practice of reporting to JFIU to obtain proper clearances to proceed with a transaction is not mentioned in the proposal. It is therefore unclear whether the practice would still be required or whether it would, somehow, be re-introduced by other means.

Some trustees are also of the view that designated authorities should be given interpretative power to give specific directions to the industries under their respective regulatory jurisdictions on how the CDD requirements should be implemented.

2. **Specific Comments to the Detailed Legislative Proposals**

2.1. ***Scope of the Legislation***

Item 1

Some trustees with an insurance background are of the view that it would not be appropriate to include insurance agencies as FIs. They believe that it would give rise to a duplication of effort if insurance agents are required to conduct another level of CDD in circumstances where insurers would already have carried out the insurers' own CDD procedures.

Under the Insurance Companies Ordinance, only authorised insurers can conduct long term business and they are the only one who can oversee all related transactions. While agents may have the chance to know about some transactions, they are merely promoters/messengers and not the true administrators of the transactions. Also, for privacy reason, agents won't be given a chance to know every transaction nor would it be justifiable for them to have access to excessive client information for CDD and record retention purpose. It would, accordingly, be inappropriate to require insurance agent to also conduct CDD.

These trustees also commented that "long term insurance business" is not defined. The term "long term business" is deemed generally to cover all insurance business including a number of classes, such as class G and H which are not really "insurance" in the literal sense. For AML purpose, the said trustees do not think it appropriate to treat insurance policies and retirement schemes as the same sort of business as they have different terminologies, structures and risk levels.

2.2. ***Circumstances when CDD is Required and the CDD Measures***

Item 3

Some trustees commented that the words "business relationship", which is not defined, would be attributed too broad an interpretation. They are also of the view that item 3(d) would not be meaningful if it gives rise to a need to do CDD in any event whether a business relationship is established or not because only after CDD has been carried out would one know whether there is suspicion of money laundering or terrorist financing.

Item 5

The same trustees are of the view that the meaning of "verifying identity on the basis of the Documents obtained from reliable and independent source" is unclear. That raises questions such as:

- (a) Would the checking of names and numbers suffice? Are we required to check on the photo against the person face-to-face?; and
- (b) Is an identity card a reliable source? And would it be considered an independent source given the fact that it is produced by the customer himself?

A better description of the required process should be included.

Trustees of discretionary trusts are of the view that the requirement in item 5(b) would be particularly problematic as the class of potential beneficiaries may be broad, or not yet known at the time of establishing the business relationship, and most importantly, may never actually benefit under the trust. The CDD measures to be taken for beneficiaries of discretionary trusts should be clarified. The definition of "beneficial owner" also need to cater for discretionary beneficiaries.

2.3. ***Ongoing Due Diligence***

Item 7

We are required to review the KYC records of all our existing customers to ensure they comply with the KYC requirements under the new legislation. Such a review must be completed within 2 years after the commencement of the new legislation. Such a review would involve a lot of time and resources. In order to save time and focus our resource on reviewing KYC records of high risk clients, we would suggest that for those customers in respect of whom simplified due diligence would be applied, a review of their KYC records would only be required upon the occurrence of a triggering event (as referred to in item 7), instead of performing the review immediately for all customers within the 2 years time-frame.

The trustees would also suggest that a separate section be included to deal with arrangements during the transition period and clearly provides for an exemption of liability in respect of existing client CDD within the first two years.

2.4. ***Simplified Due Diligence (SDD)***

Item 8

Some trustees have commented that the current drafting for simplified due diligence would not cater for those MPF or ORSO schemes the contributions to which are not deducted from employees' wage. This view is in line with the above-mentioned proposal to exempt all MPF and ORSO schemes from the CDD requirements altogether.

Trustees also suggest that the item 8(a) should also include subsidiaries of such defined FI.

2.5. ***Enhanced Due Diligence (EDD)***

Item 9

For pension funds, the identity of member is normally provided by the employer and not the employee. Accordingly, there is no face-to-face identification under those circumstances. Para (a) would therefore impose the duty of EDD on every employee member under MPF schemes (i.e. a huge portion of the working population). This is not in line with the intention of exemption under item 8. To avoid this problem, retirement scheme members should be, whether the proposal for a more general exemption as referred to in respect of item above is adopted or not, excluded from the definition of customers in this regard.

As regards the definition of "retirement schemes", they can be borrowed from the Occupational Retirement Schemes Ordinance and the Mandatory Provident Funds Schemes Ordinance.

There should be a clarification for what additional documents are required under item 9 (a)(i).

Also, there should be clarification as to whether custody services would be considered as a kind of "banking services" as referred to in this part and whether, as such, EDD is required in respect of the same.

2.6. ***Third-party Reliance /Equivalent Jurisdictions***

Item 10

The proposed legislation seems silent on the power of delegation regarding SDD and EDD. Consideration should be given to allow such delegation.

Also, para (e) (ii) (B) setting out the definition of "professional" should be clarified so that "banking" and "insurance" professionals are clearly included in that definition.

There are also suggestions for changing item 10(e) and 10(ii)(c) respectively to read as follows: "*an FI covered under this legislation and its overseas branches and subsidiaries, with the exception of RAMCs.*" and "*subject to CDD requirements to those laid down in this legislation*".

2.7. ***Customer Due Diligence in General***

Item 12

Item 12 should be made subject to item 4 to avoid any inconsistency.

Some trustees would like to see provisions for a clear exemption from any civil liability upon rejection of transactions.

In view of the serious implications to which stopping transaction or terminating a business relationship would give rise, some trustees have suggested that there should be

an option to proceed with a transaction on condition that there is no payment out until complete CDD clearance.

2.8. ***Wire Transfers and Remittance***

Item 13

There should be clarification as to whether this section applies to FIs who transfer money out for their customers and not FIs who receive the money (ie. recipients of money). Trustees are concerned about this requirement if recipient FIs is covered by it. A FI, including an insurance company, which receives money through its bank accounts, have no means to ascertain the sender's account information. The proposal is, therefore, not feasible.

2.9. ***Proposed Definitions***

"Beneficial owner"

As mentioned in 2.2 under item 5, the definition of "beneficial owner" also needs to cater for discretionary beneficiaries; even if it is to make clear that discretionary beneficiaries with unvested interests are excluded from the definition of "beneficial owner".

"Customer"

As mentioned above, the existing definition of "customers" will cover all employees under MPF schemes in Hong Kong who, in the opinion of some trustees, should not be the target of AML.

"Occasional transaction"

Some trustees are of the view that as it would disallow genuine delegation by customer of their contractual right, it is not appropriate.

We welcome further consultation and your feedback.

Yours faithfully,



Executive Committee
The Hong Kong Trustees' Association Limited