



AML Systems and Controls of Licensed Corporations

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Potential use of the securities sector for money laundering



Potential use of the securities sector for money laundering

- Illegal funds laundered through the securities sector may be generated by illegal activities both from:
 - Outside the sector: securities transactions may be used by criminals for “layering” and “integration” of money
 - Within the sector: insider trading, market manipulation, embezzlement, etc



SFC's AML supervisory framework



AML supervisory objectives

- To regulate the conduct of licensed persons engaging in securities business and monitor their compliance with relevant requirements
- To issue AML guidelines and circulars
- To investigate and take action against breaches or other misconduct
- To share information with and provide assistance to the relevant Government bureaux and departments, and other financial regulators



AML supervisory framework

- To formulate guidelines to keep pace with the latest international standards and local laws and regulations, and publish the names of designated terrorists, etc.
- To raise the awareness of the industry and provide training through seminars and a dedicated website section
- To conduct off-site monitoring and on-site inspections
- To take action against serious breaches of AML requirements



Key aspects of AML systems and controls



- Customer due diligence (CDD) and ongoing monitoring
- Record keeping
- Identification and reporting of suspicious transactions
- Staff screening, education and training



■ CDD and ongoing monitoring

- 1) Risk-based assessment
- 2) On-going due diligence
- 3) Identification of high risk customers, e.g. Politically Exposed Persons (“PEPs”) and related enhanced due diligence



■ Record keeping

- Records on transactions, both domestic and international
- Records on customer identification (e.g. copies or records of passports identity cards, driving licenses or similar documents), account files, and business correspondence



- **Recognition and reporting of suspicious transactions**
 - To be covered in next section



■ **Staff screening, education and training**

- 1) Training policies and procedures in place
- 2) Screening and training employees
- 3) Training for new and existing staff



Identification and reporting of suspicious transactions



■ **Identify suspicious transactions**

- The obligation to report under the Drug Trafficking (Recovery of Proceeds) Ordinance, the Organized and Serious Crimes Ordinance or the United Nations (Anti-Terrorism Measures) Ordinance rests with the individual who becomes suspicious of a person, transaction or property
- Appropriate measures should be taken to identify suspicious transactions in order to satisfy the legal obligations of reporting funds or property known or suspected to be proceeds of crime or terrorist property to the Joint Financial Intelligence Unit (JFIU)



- **Identify suspicious transactions**

- The most forgotten element of the CDD process
- Assess whether the transactions conducted are in line with your knowledge of the client's profile
- Put in place proper mechanisms to scrutinise transactions
- Focus should not just be on credit risk



■ **Identify suspicious transactions**

- Provide customised guidance to front line and other relevant staff
- Clear escalation procedures and reporting lines for further investigation
- Designated AML officer to take an active role
- System-generated alerts / exception reports in appropriate circumstances



- **Identify suspicious transactions**

- Third party payments

- Only requiring the client to provide certain written instructions may not be enough
- Should inquire about the reasons for the payment and the relationship between the client and the third party
- “Friends” should not be a valid relationship to justify a third party payment



Inadequate suspicious transaction reporting

- **Number of reports filed with the JFIU**

	2006	2007	2008	2009	2010	As at 10/2011
Firms registered with the SFC	121	220	242	372	662	402



Inadequate suspicious transaction reporting

- **Number of reports filed with the JFIU**
 - Despite the increase in the number of reports filed in previous years, the number of reports from the securities sector is still relatively low
 - The reports were mainly made by a relatively small number of firms



Inadequate suspicious transaction reporting

- The relatively low number of reports may be due to the following:
 - Failure to generate exception reports on large or irregular transactions
 - Failure to design suitable exception reports by reference to the suspicious transaction indicators and the specific nature of its business
 - Failure to perform timely reviews of existing customer records
 - Failure to adopt enhanced CDD measures for higher risk categories of customers
 - Failure to adopt clear escalation procedures in respect of suspicious transactions for the sake of investigation and follow-up action
 - Failure to establish clear internal guidelines for assisting staff in identifying and reporting suspicious transactions



Deficiencies identified during on-site inspections



Deficiencies identified during on-site inspections

- **Written AML policies and procedures**
 - Lack of “proper” written policies and procedures tailored to the firm’s own circumstances and AML risk exposure
- **CDD**
 - Lack of policies and procedures for identifying types of customers posing a higher risk of money laundering
 - Failure to perform timely reviews of existing customer records to re-classify the risk profiles of customers



Deficiencies identified during on-site inspections

- Identification and reporting of suspicious transactions
 - Failure by AML compliance officers to play an active part in monitoring potentially suspicious transactions and/or document the work done
 - Failure to document the assessment of potentially suspicious transactions reported by staff to the AML Compliance Officer
 - Lack of policies and procedures to deal with the money-laundering risk of third party payments and to assess whether such arrangements were suspicious transactions
 - Lack of clear and detailed policies and procedures for staff to report transactions meeting specified criteria or otherwise potentially suspicious to an appropriate designated person of the LC
 - Lack of awareness of some high risk indicators such as multiple accounts sharing the same correspondence address, which may indicate potential fraud or market misconduct and should be subject to further enquiry



Concluding remarks

- The Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance was gazetted on 8 July 2011 and will come into effect on 1 April 2012



Thank you

