SECURITIES AND
FUTURES COMMISSION
證券及期貨事務監察委員會

SFC
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AML/CFT Compliance – Potential Weakness Areas

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Ronald Mak
Senior Manager, Intermediaries Supervision, Intermediaries

Ivan Wan
Manager, Intermediaries Supervision, Intermediaries

Disclaimer

Where this presentation refers to certain aspects of the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance (AMLO) and the guidelines on AML/CFT published by the SFC, it provides information of a general nature that is <u>not</u> based on a consideration of specific circumstances. Furthermore, it is <u>not</u> intended to cover all requirements that are applicable to you and your firm. Accordingly, it should not be regarded as a substitute for seeking detailed advice on any specific case from your own professional adviser.

Outline

A. Introduction

B. Deficiencies and weaknesses in internal AML/CFT policies, procedures and controls

C. Transactions monitoring and suspicious transactions reporting

A. Introduction

Introduction

- Highlight some potential weakness areas in LCs' AML/CFT control systems identified by the SFC
- Remind LCs of the applicable requirements of the AMLO, AML Guideline or other law/regulation
- Remind LCs of the importance of transactions monitoring and suspicious transactions reporting

B. Deficiencies and weaknesses in internal AML/CFT policies, procedures and controls

AML/CFT systems

AML/CFT systems (Policies, Procedures and Controls)

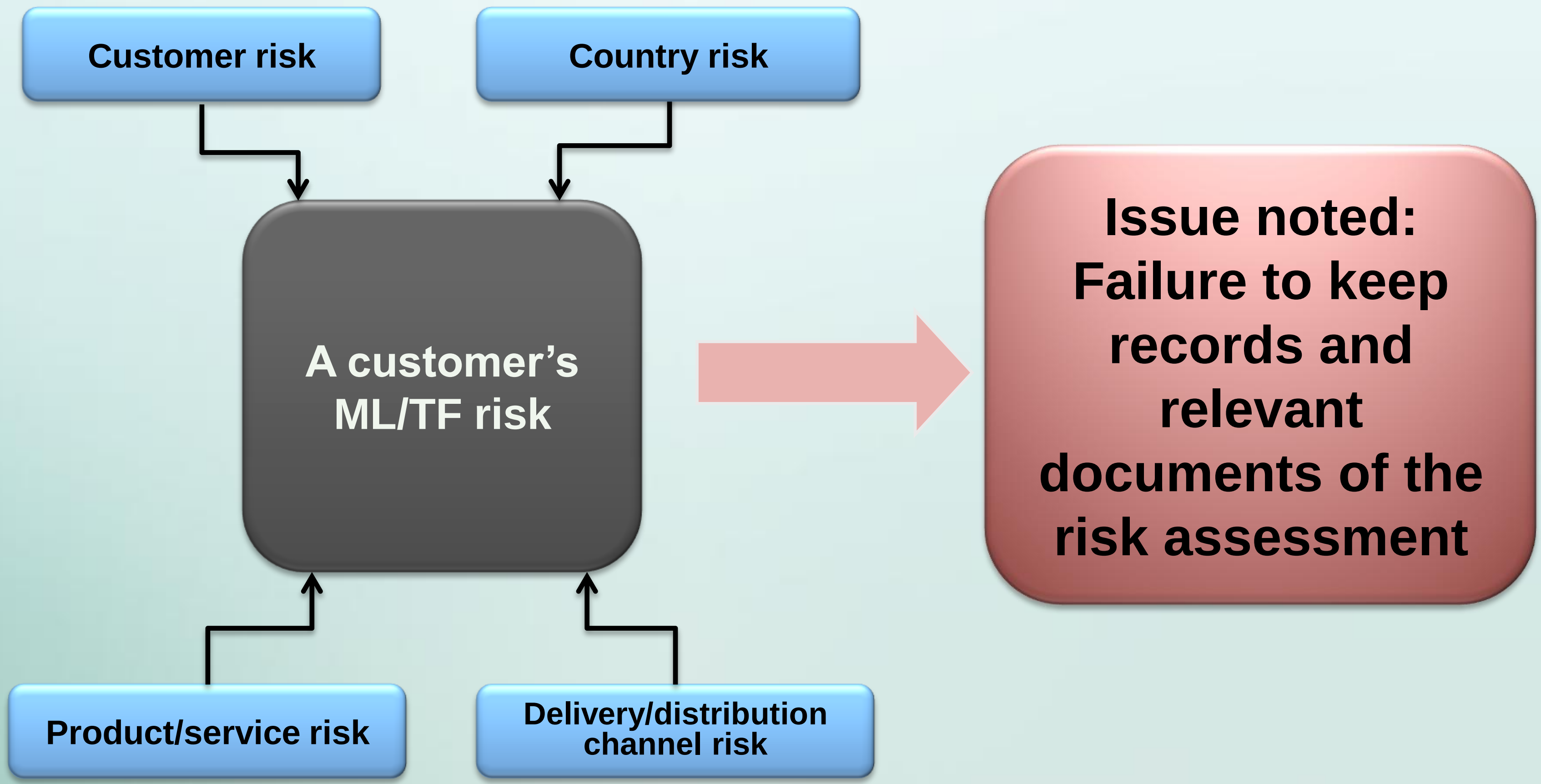
Deficiencies and weaknesses:

1. Inadequate customer risk assessment
2. Inadequately detailed AML/CFT policies and procedures
3. Failure to implement certain AML/CFT requirements

1

Customer risk assessment

Paragraphs 3.5 – 3.8 of the Guideline

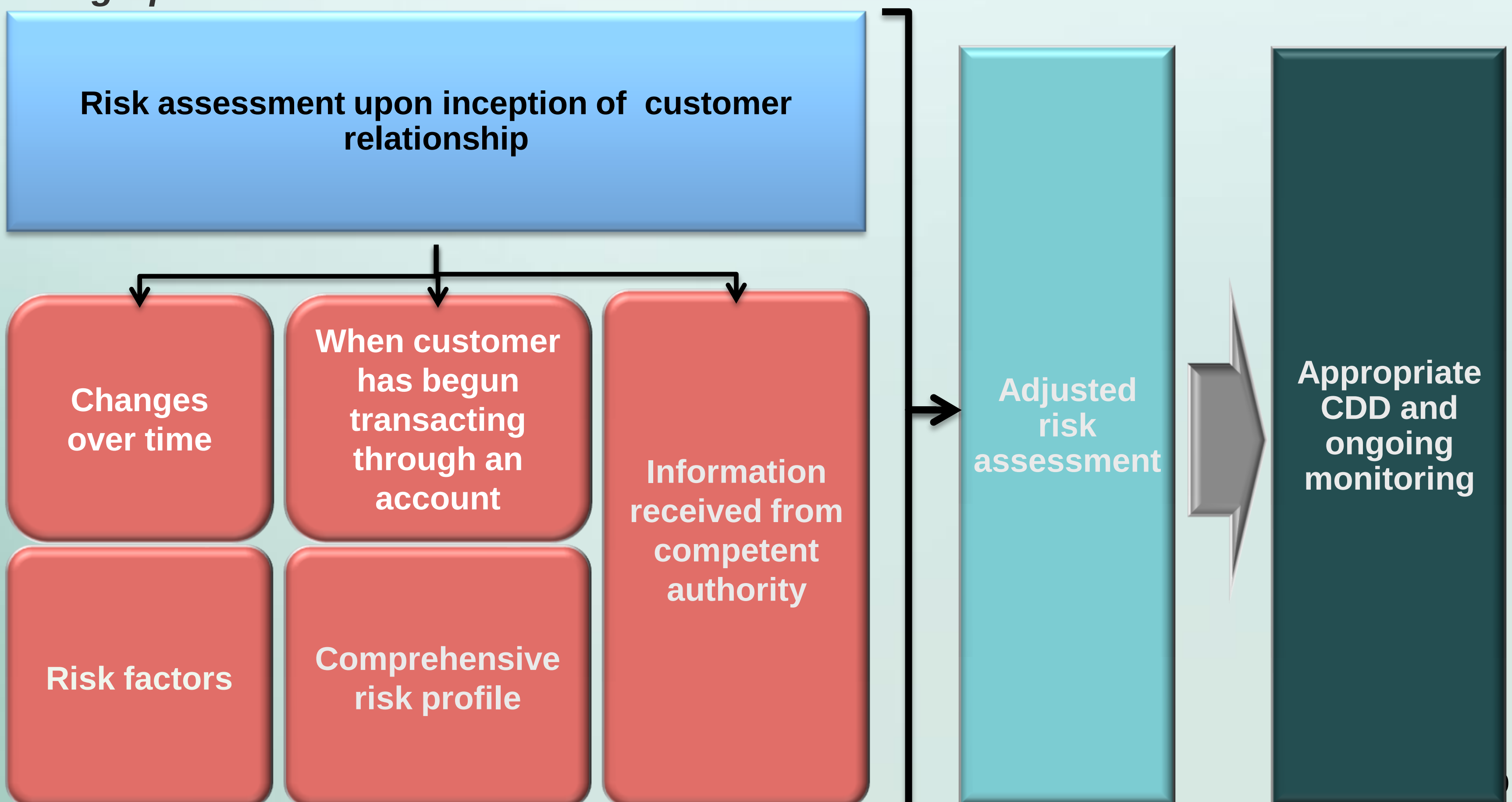


1

Ongoing review

- Issue noted:
  - Failure to review whether the risk assessment of a particular customer needs adjustment upon subsequent changes of the customer’s risk profile

Paragraph 3.6 of the Guideline



1

CDD - Person purporting to act on behalf of the customer

Issue noted: Failure to take into account customers' ML/TF risk to determine whether application of a streamlined approach is appropriate

Guidance provided in paragraph 4.4.4 of the Guideline on when a streamlined approach may be sufficient

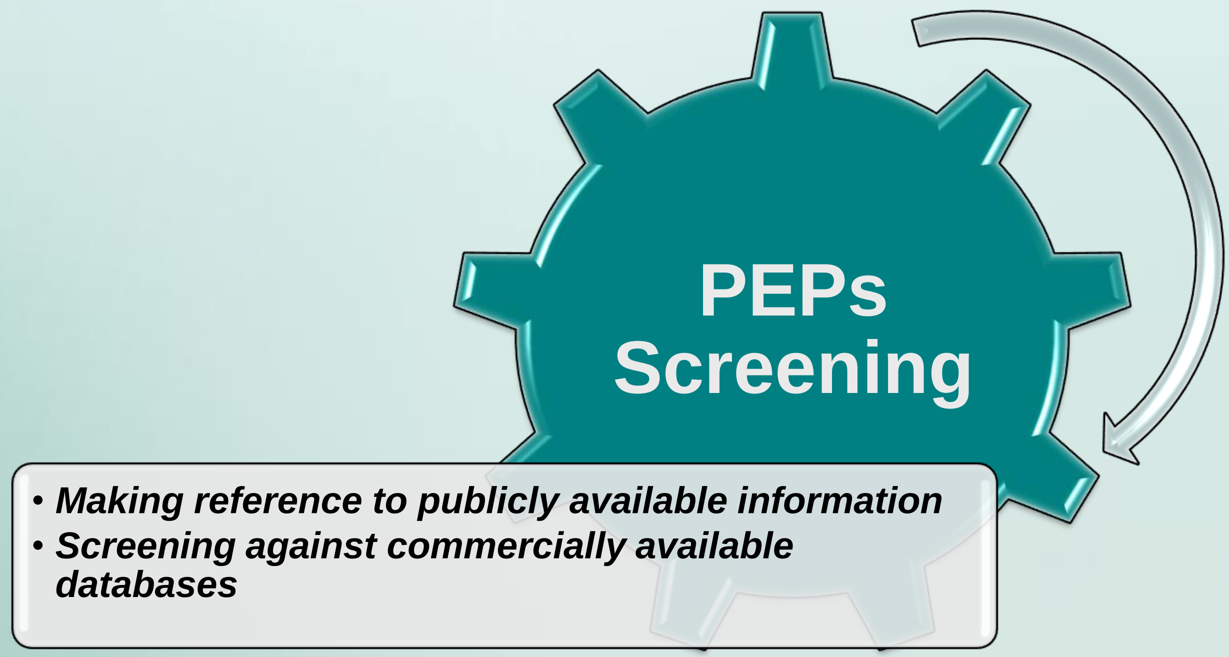
Where streamlined approach cannot be applied, LCs should *(Paragraphs 4.4.1 – 4.4.3 of the Guideline)* -

Identify and take reasonable measures to verify the identity of the person purporting to act on behalf of the customer: (a) full name; (b) date of birth; (c) nationality; and (d) ID type and number	Verify the person's authority by obtaining a board resolution or similar written authority

CDD – politically exposed persons (“PEPs”) screening

- Issues noted:
  - Inadequate PEPs screening procedures
  - Solely relying on the background information provided by the customers

Paragraphs 4.13.9 and 4.13.15 of the Guideline



2

CDD – PEPs screening (continued)

- Majority of LCs conducted PEPs screening via various means and a small portion of LCs did not have any screening
- Examples of data sources for PEPs screening include:

Documents provided by the customer and/or information provided by referee

Internally developed database, third-party vendor database, and/or online search engine

2

On-going monitoring

- Issue noted:
  - Failure to monitor transactions that are complex, large, unusual, or patterns of transactions which have no apparent economic or lawful purposes, for suspicious transactions

Cash deposits broken down into multiple smaller amounts

Frequent receipts from unverified third parties

Deposits and withdrawals of large amount on the same day

Deposits and withdrawals without any transactions

2

On-going monitoring (continued)

Examples of exception reports

- Identify customers with changing transaction pattern through the comparison of monthly turnover of consecutive months
- Identify customers with large fund deposit/withdrawal
- Identify cash receipt

Paragraph 5.9 of the Guideline

- **Methods to monitor customer transactions and activities include exception reports and transaction monitoring systems.**

3

CDD - Keeping customer information up-to-date

- Issues noted:
  - Failure to undertake periodic reviews of existing records of customers upon certain triggering events
  - Failure to review the profile of all high risk customers at least on an annual basis

Paragraph 4.7.12 of the Guideline

a significant transaction is to take place	**material change occurs in the way the customer's account is operated**	**the FIs customer documentation standards change substantially**	**the FI is aware that it lacks sufficient information about the customer concerned**

3

CDD - Conducting company search

- Issue noted:
  - Failure to obtain company search report, certificate of incumbency or equivalent for corporate customers to confirm whether the company is still registered, independently identify and verify the names of the directors and shareholders, etc.

Paragraph 4.9.11 of the Guideline

Locally incorporated company

- **Company search report**

Overseas incorporated company

- **Company search report**
- **Certificate of incumbency**
- **Similar or comparable document**

3

CDD - Jurisdiction equivalence

- Issue noted:
  - Failure to perform/document the assessment of jurisdiction equivalence of non-FATF members

Paragraph 4.20.3 of the Guideline

Factors to be considered

- mutual evaluation reports
- jurisdictions published in the FATF statement
- advisory circulars issued by SFC
- lists of jurisdictions, entities and individuals published by specialised national, international, non-governmental and commercial organisations.

3

Financial sanctions and terrorist financing

- Issue noted:
  - Failure to screen customers against financial sanctions and terrorist financing

Paragraphs 6.20 and 6.22 of the Guideline

Internal database maintained by FI

OR

Database maintained by third party service provider

Comprehensive ongoing screening

screen customers against current terrorist and sanction designations at the establishment of the relationship

new terrorist and sanction designations published by the SFC are screened against entire client base

3

Monitoring and reporting of suspicious transactions

- Issues noted:
  - Failure to make report on further suspicious transactions of the same nature of the previous suspicion to the JFIU
  - Failure to timely report suspicious transactions to the JFIU

Paragraphs 7.27, 7.30 – 7.32 of the Guideline

Keep relevant documentation of reports made to MLRO and JFIU

3

Suspicious transaction reports

- Issue noted:
  - Failure to review the business relationship after filing report to JFIU
- FIs should ***(Paragraph 7.33 of the Guideline)***:

note that a “consent” response from the JFIU to a pre-transaction report should not be construed as a “clean bill of health”

conduct an appropriate review of a business relationship upon the filing of a report to the JFIU and if necessary the issue should be escalated to the FI’s senior management

take appropriate action to mitigate the risks, once an FI has concerns over the operation of a customer's account or a particular business relationship

3

Staff training

- Issue noted:
  - Failure to provide sufficient training to staff to maintain their AML/CFT knowledge and competence

Paragraph 9.7 of the Guideline

AML training program				
All new staff (para 9.7(a))	Staff who deal directly with the public (para 9.7(b))	Back-office staff (para 9.7(c))	Managerial staff including internal audit officers and COs (para 9.7(d))	MLROs (para 9.7(e))

3

Staff training

- Issue noted:
  - Failure to keep training record for a minimum of 3 years

Paragraph 9.9 of the Guideline

Training records for 3 years → *Who attended* → *When organized* → *Type of the training*

AML/CFT Self-Assessment Checklist

The AML/CFT Self-Assessment Checklist has been prepared to provide a structured framework for LCs and AEs to assess compliance with key AML/CFT requirements.

LCs and AEs are advised to use this as part of their regular review to monitor their AML/CFT compliance.

The frequency and extent of such review should be commensurate with the risks of ML/TF and the size of the firm's business.

LCs and AEs should ensure that any compliance deficiencies identified during the regular reviews are rectified in a timely manner.

AML/CFT Self-Assessment Checklist

Other publications and information sources | Securities & Futures Commission of Hong Kong - Windows Internet Explorer

http://www.sfc.hk/web/EN/rule-book/anti-money-laundering-and-counter-terrorist-financing/other-publications-and-information-sources.html

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Other publications and information sources

Training materials

1. Introduction to money laundering ("ML") / terrorist financing ("TF") (August 2007)
2. Legislation concerned with money laundering and terrorist financing (August 2007)
3. Recognition and reporting of suspicious transactions (Revised in March 2012)
4. Potential use of securities and futures sector in ML / TF process (Revised in March 2012)
5. Anti-Money Laundering Training Seminar 2011 (Revised in March 2012)
6. Briefing Seminar on the New Guidelines on Anti-Money Laundering and Counter-Terrorist Financing 2012 (February 2012)
7. Anti-Money Laundering and Counter-Terrorist Financing Seminar 2012 (October 2012)

AML/CFT Self-Assessment Checklist

- AML/CFT Self-Assessment Checklist

Archives - Guidelines & Self-assessment Survey & Training Materials

- Prevention of Money Laundering and Terrorist Financing Guidance Note (September 2009) [this was superseded on 1 April 2012 by the AML/CFT Guideline and AE Guideline]
- Self-assessment Survey (2007) [Cancelled]
- Training materials [Cancelled]

C. Transactions monitoring and suspicious transactions reporting

Criminal liability for non-compliance of DTROP, OSCO and UNATMO

Sections 25A of the Drug Trafficking (Recovery of Proceeds) Ordinance ("DTROP")

Sections 25A of the Organized and Serious Crimes Ordinance ("OSCO")

Section 12 of the United Nations (Anti-Terrorism Measures) Ordinance ("UNATMO")

It is an offence to fail to disclose where a person knows or suspects that property represents the proceeds of drug trafficking or of an indictable offence or terrorist property respectively

Criminal liability for non-compliance of DTROP, OSCO and UNATMO

Paragraphs 7.2 – 7.3 of the Guideline

Filing a report to the JFIU provides FIs with a statutory defence to the offence of ML/TF in respect of the acts disclosed in the report, provided:

- the report is made before the FI undertakes the disclosed acts and the acts (transaction(s)) are undertaken with the consent of the JFIU; or
- the report is made after the FI has performed the disclosed acts (transaction(s)) and the report is made on the FI's own initiative and as soon as it is reasonable for the FI to do so.

Once an employee has reported his suspicion to the appropriate person in accordance with the procedure established by his employer for the making of such disclosures, he has fully satisfied the statutory obligation.

Suspicious transactions reports

Identify suspicious transactions

- 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

Importance of monitoring and reporting suspicious transactions

Number of reports filed with the JFIU

	2007	2008	2009	2010	2011	2012	As at 10/2013
Firms registered with the SFC	220	242	372	662	470	698	1,123

Importance of monitoring and reporting suspicious transactions

Number of reports filed with the JFIU

- Despite the increase in the number of reports filed, the number of reports from the securities sector is still low compared to the banking sector (2012: 19,202; 2011: 17,194; 2010: 16,551; 2009: 12,602) and the money services provider sector (2012: 1,171; 2011: 1,051; 2010: 1,667; 2009: 2,701).
- The reports were mainly made by a relatively small number of firms.

Examples of suspicious transactions

Paragraph 7.14 of the Guideline

- The following is a (non-exhaustive) list of examples of situations that might give rise to suspicion in certain circumstances:

transactions or instructions which have no apparent legitimate purpose and/or appear not to have a commercial rationale

where the transaction being requested by the customer, without reasonable explanation, is out of the ordinary range of services normally requested, or is outside the experience of the financial services business in relation to the particular customer

unnecessary routing of funds or other property from/to third parties or through third party accounts

Examples of suspicious transactions

- LCs are reminded to have effective AML system to combat laundering of proceeds of tax evasion, which constitutes as an indictable offence in Hong Kong. Where LCs have knowledge or suspicion of tax evasion related activities, they should report to JFIU as appropriate.
- For example, LCs should be aware of the involvement of offshore companies on whose accounts multiple transfers are made, especially when they are destined for a tax haven, and to accounts in the name of offshore companies of which the customer may be a shareholder.
- Further examples of what might constitute suspicious transactions are provided in paragraphs 7.39 – 7.40 of the Guideline.

Thank you