



*The article is for general information only and is not intended to constitute legal or other professional advice.*

## **Anti-Money Laundering and Counter Terrorist Financing (“AML/CTF”) – An enforcement alert**

On 1 April 2012, the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance (Cap. 615) (“AMLO”) was effective to prohibit the act of money laundering. Meanwhile, the SFC has issued a Guideline on Anti-Money Laundering and Counter-Terrorist Financing (“AML guideline”) so as to offer Licensed Corporations (“LCs”) guidance to meet the AMLO and other relevant legal and regulatory requirements. Some LCs may not incorporate the AMLO and the AML guideline into their everyday business activities. This, in turn, may have resulted in LCs taking the circulars and guidelines as a mere symbolic gesture by the SFC, with no fear of actually being caught. The recent SFC enforcement actions on four LCs during the period of March – April 2017 serves as an important and serious alert that it is time for all LCs to review and improve their internal AML/CFT policies.

### ***Common deficiencies and failures of AML controls***

#### **(1) Allowing Third-Parties Transactions Without Proper Assessment**

With regards to the recent SFC enforcement actions, the lack of scrutiny on third party transactions appeared to be a reoccurring theme. One of these cases is Zhongtai International Securities Limited (SFC Type 1 and 4 LC) (“Zhongtai”).

Case Link: <http://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/enforcement-news/doc?refNo=17PR32>

Between the period of January 2013 and December 2014, Zhongtai has processed over 300 third party transactions without any prior assessment on them. In addition, Zhongtai accepted these deposits even:

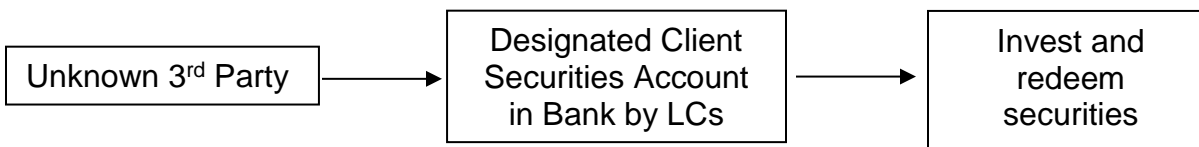
- (a) The source and the identity of the third party deposits were not clearly identified and clarified;
- (b) The third parties failed to give reasonable explanations behind their deposits. For instance, being mere “friends” was usually accepted in justifying the relationship between the third party and client; and/or

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(c) Some third-party deposits were of a particularly substantial amount so as to raise suspicion.

Therefore, the SFC believes Zhongtai has violated Section 5(1) of Appendix 2 under the AMLO and also the monitoring responsibility as described under Sections 5.1, 5.10 and 5.11 of the AML guideline.



**Note: The offenders can achieve money laundering through deposits into client securities account with purchase and sales of their investments later (e.g. stocks). This explains why the SFC concerns third party transactions and imposes a stricter requirement regarding the relevant controls.**

## (2) Lack of adequate compliance procedures and/or proper compliance functions

In addition, the SFC also identified and took action against LCs that did not have sufficient AML policies and regulatory mechanisms in place. An apparent example is the case of iSTAR International Futures Co. Limited (SFC Type 2 LC) (“iSTAR”).

Case Link: <http://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/enforcement-news/doc?refNo=17PR48>

The SFC criticized iSTAR for its failure in developing and maintaining an effective compliance procedure for processing third party transactions. It was discovered in this case that iSTAR had designated their Administration and Human Resources Manager as their AML Compliance Officer from February 2014 to August 2014. This, in turn, strongly suggested that iSTAR failed to have proper functional compliance and AML procedures in place during that time.

## (3) Unexecuted AML/CFT policies

An LC’s evidence in having a proper internal AML/CFT policy does not release them from SFC’s radar. LCs must ensure that these policies are properly acknowledged by staff members and implemented into the business.

For instance, Guoyuan Securities Brokerage (Hong Kong) Limited (SFC Type 1 and 4 LC) (“Guoyuan”) claimed that their compliance manual covered relevant AML/CFT compliance procedures.

Case Link: <http://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/enforcement-news/doc?refNo=17PR43>

However, it was discovered that Guoyuan’s staff members and responsible officers were completely unaware of the existence of this compliance manual. This indicated to SFC that since the staff members had no knowledge, it was likely that they failed to properly observe the AML/CFT requirements, and hence Guoyuan has failed to meet its legal and regulatory obligations tailored to

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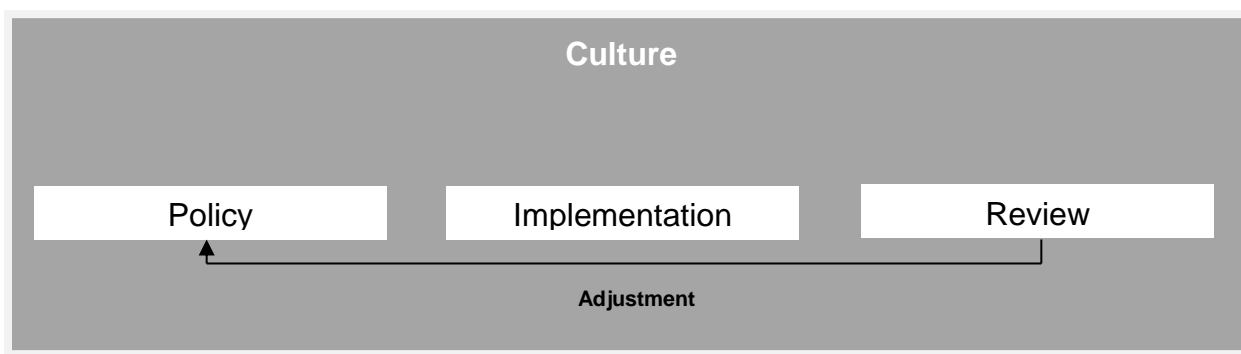
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the company's particular business risk profile.

## ***Time to get equipped***

The SFC has clearly expressed that AML/CFT compliance will continue to be a focus of the SFC's supervision of LCs and AEs in the coming year. The SFC will take regulatory actions and initiate enforcement proceedings against firms found to have breached AML/CFT requirements.

Therefore, LCs should stay vigilant and use the guidelines to assist them in their senior management in designing and implementing their own policies, procedures and controls in their relevant operational areas, taking into consideration their special circumstances so as to meet the relevant AML/CFT statutory and regulatory requirements.



LCs can consider the above "CPIR model" in order to set up the AML controls. It will be elaborated below.

## **C - Culture**

It is of utmost importance to nurture an AML compliance culture. It is impossible for the compliance staff to maintain and implement any AML rules if the senior management and responsible officers are not cooperative.

## **P - Policy**

LCs are advised to develop or review their existing AML standards. They can start by reviewing the existing AML rules, including the AMLO and the AML guidelines as issued by the SFC. The SFC has also indicated that the LCs from the abovementioned case examples violated section 5.10 of the AML guideline, which states:

*"Where transactions that are complex, large or unusual, or patterns of transactions which have no apparent economic or lawful purpose are noted, FIs should examine the background and purpose, including where appropriate the circumstances, of the transactions."*

It reminds LCs to determine whether the transaction monitoring controls, due diligence and Know-Your-Client process is enough when developing their own AML programs specific to their organizational and legal structure.

## **I - Implementation**

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After execution of the AML policies, LCs should think about the following questions:

- (a) Can LCs fulfill the relevant personnel requirements to handle the AML compliance?
- (b) Is there a clear division of work within the LCs?
- (c) Will any additional AML resources be adopted? This includes the client identity check system and transaction monitoring software; And
- (d) Has the LCs offered sufficient and appropriate AML training that will ensure staff members will understand and abide by the AML regulatory and internal requirements?

The LCs should document the relevant AML check records for internal review and regulatory review, including the SFC's inspection, so as to demonstrate that they can properly execute their AML/CFT programs.

## **R - Review**

Lastly, there should be a regular review of these AML policies and procedures in terms of their effectiveness. The SFC has also issued an AML/CTF self-assessment checklist which provides guidance on such self-review

Checklist Link:

[http://www.sfc.hk/web/EN/files/IS/AML/SELF\\_ASSESSMENT\\_CHECKLIST\\_ENG.xlsx](http://www.sfc.hk/web/EN/files/IS/AML/SELF_ASSESSMENT_CHECKLIST_ENG.xlsx)

In particular, if part of the AML functions were delegated to a third party, they should be regularly assessed and monitored.

The LCs should also stay tuned on the Circulars and Enforcement News as announced from the SFC, especially the Circular to LCs and Associated Entities - Anti-Money Laundering / Counter Financing of Terrorism ("AML/CFT") - Compliance with AML/CFT Requirements so as to avoid the repeating mistakes.

Circular Link: <http://www.sfc.hk/edistributionWeb/gateway/EN/circular/doc?refNo=17EC9>

If you have any further questions regarding this issue of CP insights or have any topic you would like us to cover, please submit your response here <https://goo.gl/forms/gDLVThTmxGvMI4r12>.

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