



Financial Action Task Force

Groupe d'action financière

SUMMARY

**OF THE THIRD MUTUAL EVALUATION REPORT
ON ANTI-MONEY LAUNDERING AND
COMBATING THE FINANCING OF TERRORISM**

HONG KONG, CHINA

20 JUNE 2008

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THIRD MUTUAL EVALUATION OF HONG KONG, CHINA

EXECUTIVE SUMMARY

1. Background Information

1. This report provides a summary of the anti-money laundering (AML) and combating the financing of terrorism (CFT) measures in place in Hong Kong, China (hereinafter Hong Kong) at November 2007 (the date of the on-site visit) and immediately thereafter. It describes and analyses those measures and provides recommendations on how certain aspects of the system could be strengthened. It also sets out Hong Kong's level of compliance with the Financial Action Task Force (FATF) *40+9 Recommendations* (see attached table *Ratings of Compliance with the FATF Recommendations*).

2. Hong Kong is a special administrative region of the People's Republic of China (PRC). According to the design of the *Basic Law*, which is Hong Kong's constitutional document, the political structure is basically an executive-led system headed by a Chief Executive. Hong Kong also has a Legislative Council, the powers and functions of which include enacting, amending and repealing laws in accordance with the provisions of the *Basic Law* and legal procedures. It is a common law legal system and the independence of the judiciary is enshrined in the *Basic Law*. Hong Kong is an international financial centre with over 200 banking institutions and vibrant insurance and securities sectors. Authorities are not able at this time to determine the volume of money laundered in or through Hong Kong. The laundering of drug proceeds has declined in recent years and is increasingly derived from trafficking for domestic use. The primary domestic sources of laundered funds in Hong Kong are illegal gambling, fraud and financial crime, loan sharking and vice. The availability of corporate services and the relative ease with which shell companies can be purchased contribute to the risk of Hong Kong being used for structuring of the proceeds of financial crime, corruption, tax evasion and smuggling. Investigations have found no evidence of terrorist funds moving through Hong Kong.

3. Hong Kong has a good legal structure to combat money laundering (ML) and terrorist financing (TF). The ML offence, established in 1989 and expanded in 1994, is broad and almost fully meets the FATF requirements. It is well prosecuted with a satisfactory conviction rate. The terrorist financing offence in the *United Nations (Anti-Terrorism Measures) Ordinance* is less expansive as it does not cover provision/collection for an individual terrorist or terrorist organisation. In addition, the offence applies to 'funds' but not non-financial assets and does not extend to terrorism directed towards international organisations. Terrorist funds have not been detected in Hong Kong and there have been no prosecutions for TF. While Hong Kong has a workable and fairly comprehensive criminal confiscation regime, these measures are not available in all cases, do not extend to all predicate offences and the number of confiscations is relatively low. While legislative provisions have been enacted for confiscation of the proceeds of TF, these provisions are not yet in force. Hong Kong's financial intelligence unit is effective and is the focal point for Hong Kong's law enforcement efforts to combat ML and TF. It and other competent authorities have been designated responsibility for investigation and prosecution of ML and TF offences. Measures for domestic and international co-operation are generally effective.

4. The preventive system addresses customer identification and other AML/CFT obligations and applies to a range of financial institutions and some designated non-financial businesses and professions (DNFBPs) as defined by the FATF. There are relatively limited requirements in place for remittance agents, money changers, money lenders (including those financial factoring businesses which are not

‘authorised institutions’, *i.e.* banking institutions), credit unions, the post office and financial leasing companies¹. A number of the AML/CFT obligations exist only in mandatory guidelines issued by the regulatory authorities which are generally comprehensive and constitute other enforceable means. The preventive system for some non-core financial institutions does not incorporate adequate customer due diligence (CDD) requirements with respect to politically exposed persons. While the volume of suspicious transaction reports (STRs) has increased in recent years, the submission of STRs by DNFBPs could be improved. Sound requirements as to internal controls and compliance functions are in place for core financial institutions (banking, securities and insurance). Supervision is effective for the banking, insurance and securities sectors, but weak or non-existent for many types of DNFBPs. The range of sanctions available for AML/CFT breaches is broad for core financial institutions other than insurance and is appropriately employed by the supervisory authorities.

2. Legal System and Related Institutional Measures

5. The offence of ML related to drug trafficking was enacted in 1989 under the *Drug Trafficking (Recovery of Proceeds) Ordinance* and its application broadened by a complementary ML offence in the 1994 *Organized and Serious Crimes Ordinance*. The ML offence implements the elements of the *Vienna* and *Palermo* Conventions. Whilst predicate offences in Hong Kong generally cover a broad ambit of offences within each of the designated categories of offences, the range of environmental crimes that constitute predicate offences is limited. The offence of ML extends to any property that constitutes criminal proceeds, regardless of value, and a broad range of ancillary offences attaches to it. The ML offence applies to natural and legal persons, though there have not been any prosecutions of legal persons for ML. The ML offence is well prosecuted with a satisfactory conviction rate. The maximum penalties available for ML offences are appropriately high. The sentencing starting point for ‘more serious’ cases sits at four to six years’ imprisonment, in line with sentences passed for ‘mid-tier’ frauds.

6. Terrorist financing was criminalised under the *United Nations (Anti-Terrorism Measures) Ordinance* (UNATMO) in 2002, however the offence is narrow in scope and certain key provisions of this ordinance are not yet in force. Certain provisions within the *United Nations Sanctions (Afghanistan) Regulation* (UNSAR) also make it an offence to make funds or other financial assets available to listed entities. The TF offence under UNATMO does not cover provision/collection for an individual terrorist or terrorist organisation and the offence under UNSAR extends only to those individuals and entities designated by the 1267 Committee. The TF provision does not apply where the terrorism is directed at an international organisation or where the financing is in the form of assets other than ‘funds’. Its applicability is also subject to ‘civil dissent’ exceptions of potentially broad reach. As noted above, Hong Kong has not, to date, brought any TF prosecutions.

7. Hong Kong has a workable and fairly comprehensive criminal forfeiture regime. Restraint and confiscation provisions are limited in their availability as they can be used only for those indictable offences listed in the *Organized and Serious Crimes Ordinance* (OSCO) and restraint may only occur where the amount involved is over HKD 100 000 (USD 12 800). Some types of instrumentalities are subject to forfeiture. No provisions are in place for forfeiture of proceeds/instrumentalities of terrorist acts or TF². Given the risk of money being laundered in Hong Kong (including proceeds of foreign predicate offences), the number of restraint orders is low. An enhanced focus on confiscation began in 2007 to

¹ Credit unions in Hong Kong are co-operative organisations in which the available deposit and lending mechanisms are limited. Hongkong Post provides postal remittance services and acts as an agent for Western Union.

² Provisions for forfeiture of proceeds/instrumentalities of terrorist acts or TF have been enacted but are not yet in force.

increase the numbers of restraint and confiscation applications sought and granted and to ensure that Hong Kong administers an effective regime for confiscation of the proceeds of ML and TF.

8. It is an offence to make funds available to entities in accordance with United Nations Security Council Resolution 1267. Hong Kong relies on an offence of ‘making available’ property to terrorists and has not implemented an express freezing provision to fully implement this UN Resolution with respect to assets already under the control of designated entities. Similarly, Hong Kong has not implemented the freezing obligations imposed by United Nations Security Council Resolution 1373. In addition, Hong Kong does not have a system for examining and giving effect to actions initiated under freezing mechanisms of other jurisdictions³. No terrorist assets have been frozen in Hong Kong pursuant to these UN Resolutions.

9. The Joint Financial Intelligence Unit (JFIU) was established following the introduction of the *Drug Trafficking (Recovery of Proceeds) Ordinance* in 1989. The JFIU is a law enforcement unit housed within the Hong Kong Police Force (the Hong Kong Police) and staffed primarily by police officers, but also by Customs & Excise Department (C&ED) officers. It is Hong Kong’s centre for receiving and requesting, analysing and disseminating disclosures of STRs and other relevant information concerning suspected ML or TF activities. The JFIU has broad access to information and is able to seek additional information from reporting parties. It also has the full range of investigative powers granted to the Hong Kong Police and the C&ED. Information held by the JFIU is securely protected and disseminated only in accordance with the laws of Hong Kong. In 2006, the JFIU significantly enhanced its IT capacity for: online receipt of STRs; analysis of STRs; and, storage of information and intelligence contained in and developed from the STRs. Information is disseminated to domestic and international authorities when there are grounds to suspect ML or TF. The JFIU and the Narcotics Division of the Security Bureau provide outreach to financial institutions and DNFBPs to enhance awareness of STR reporting and other ML and TF compliance requirements and provides guidance regarding the manner of reporting. Overall, the action it has taken has been proactive and effective. In addition to its core functions, the JFIU has a mandate to register remittance agents and money changers (RAMCs).

10. Hong Kong has designated authorities to investigate ML and TF offences and has equipped them with necessary powers. The primary investigative authorities are the Hong Kong Police, the C&ED and the Independent Commission Against Corruption. The Hong Kong Police is the primary enforcement authority for ML and TF investigations. All three of these agencies have permanent special investigative groups dedicated to investigations of ML and TF and are mandated to investigate, seize, freeze and confiscate the proceeds of crime. Hong Kong enforcement authorities have access to a range of special investigative techniques when conducting ML or TF investigations and may compel production, search and seizure of documents. Hong Kong’s Department of Justice provides legal advice to the government, conducts criminal prosecutions, manages asset recovery and is the focal point for mutual legal assistance.

11. Hong Kong has not implemented a declaration or disclosure system to detect, seize or confiscate the physical cross-border transportation of currency or bearer negotiable instruments that are related to ML or TF. Law enforcement agencies can use their general powers to target travellers on an intelligence basis, though the number of ‘disclosures’ received in this way is extremely small.

³ Provisions establishing a freezing mechanism to implement S/RES/1737(2001) and a mechanism to give effect to freezing mechanisms of other jurisdictions have been enacted but are not yet in force.

3. Preventive Measures - Financial Institutions

12. The Hong Kong government has taken measures to actively encourage development and use of modern and secure techniques for financial transactions which are less vulnerable to money laundering. It is general government policy not to stand in the way of the development of electronic money and to develop a regulatory framework which provides a sound and secure basis for the continuous development of electronic money.

13. The application of Hong Kong's AML/CFT measures to the financial system and to DNFBPs is not based on a risk assessment in the manner contemplated in the revised *FATF Recommendations*. Most financial activities are conducted by institutions that are authorised and supervised by the three primary regulatory authorities: the Hong Kong Monetary Authority (HKMA), the Securities and Futures Commission (SFC) and the Office of the Commissioner of Insurance (OCI). All three regulatory authorities issue mandatory guidance which is considered to be other enforceable means, as well as other non-binding guidance. The guidance issued to the banking, securities and insurance institutions covers a broad range of AML/CFT matters. Other types of institutions which also provide financial services are subject to relatively limited AML/CFT obligations and oversight, despite the absence of any formal assessment to justify their exclusion from AML/CFT obligations. These are: remittance agents, money changers, money lenders (including financial factoring businesses), credit unions, the post office and financial leasing businesses⁴.

14. A number of important CDD requirements exist in the enforceable guidelines issued by the regulatory authorities rather than in law or regulation. Banking, securities and insurance entities must identify and verify the identity of customers, including any beneficial owners, before establishing a business relationship. Only basic CDD obligations are in place for money remitters and money exchange companies and there are no CDD obligations for money lenders, credit unions and financial leasing companies. The banking and insurance guidelines impose obligations on banking and insurance institutions to exercise enhanced due diligence with respect to politically exposed persons. These guidelines do not specify that senior management approval is required to continue a business relationship with a customer discovered to be a politically exposed person, though some other provisions in those guidelines can be considered to have a similar effect in practice.

15. The scope of permissible reliance on third-party introductions within the banking and securities sectors is broad in terms of the type of introducer from whom the introduction may be accepted, and the country of origin of the introducer. In the banking and securities sectors, reliance may be placed on introducers who are not regulated for AML/CFT purposes. There are no financial institution secrecy provisions that inhibit the implementation of the *FATF Recommendations* within the regulated sectors. Access to and sharing of information is permitted under the respective ordinances that govern the banking, securities and insurance sectors. However, access to information for the non-regulated sectors, including remittance agents, is limited in scope.

16. General record-keeping requirements are embedded in law/regulation. The mandatory guidelines issued by the regulatory authorities supplement this by requiring the banking, securities and insurance sectors to maintain all transaction records for at least six years, to facilitate the reconstruction of individual transactions and to make such records available to the regulatory authorities upon request. In the banking and insurance sectors, customer identification records, account files and business correspondence must be kept for more than six years. Record-keeping requirements for the remittance agents are incomplete and, as there is no regulator for that sector, the level of implementation of record-keeping requirements by this

⁴ Insofar as money lenders, credit unions, the post office and financial leasing businesses are concerned, the impact of this on the ratings is minimal, in view of the relatively limited scale of the activities of these institutions.

sector cannot be determined. Obligations imposed on financial institutions with respect to information which must be transmitted along with wire transfers are comprehensive. There are no requirements for remittance agents or the Hongkong Post to transmit full originator information in the message or form accompanying the wire transfer.

17. Financial institutions are obliged to pay attention to complex unusual large transactions, or unusual patterns of transactions, which have no apparent or visible economic or lawful purpose. The existing guidance for banks requires them to maintain management information systems for identification of unusual transactions and to review the reports generated by these systems. However it does not require banks to document their analyses of transactions that are regarded as unusual⁵. Hong Kong has a system for ensuring that financial institutions are advised of concerns about weaknesses in the AML/CFT systems of other countries or for ensuring that financial institutions are notified, where necessary, of the need to apply countermeasures. There are no requirements for remittance agents, money changers, money lenders, credit unions or financial leasing companies to pay attention to unusual transactions or to give special attention to business relationships and transactions with persons from or in countries which do not or insufficiently apply the *FATF Recommendations*.

18. Hong Kong legislation provides clear and broad obligations for reporting suspicious transactions, with associated protection from civil or criminal liability when complying with the reporting obligation. Every legal and natural person in Hong Kong is obliged to report suspicious transactions and those who do report are protected from civil or criminal liability when complying with the reporting obligation. Financial institutions and their directors, officers and employees are prohibited from disclosing the fact that an STR has been submitted to the JFIU, but this prohibition does not apply in all cases where an STR is being considered but has not yet been submitted to the JFIU. The reporting obligation suffers from the limitations in the terrorist financing offence and from the incomplete coverage of one of the required types of predicate offences (environmental crimes). The JFIU actively provides guidance and feedback to the reporting entities, including statistics on the STRs received as well as information on the latest money laundering trends and typologies.

19. Internal control procedures, compliance and independent audit functions, employee screening and training obligations are in place in the banking, securities and insurance sectors, but not for remittance agents, money changers and money lenders. The banking, securities and insurance guidelines require domestically-incorporated institutions to apply the Hong Kong AML/CFT standards to their overseas branches and subsidiaries. Where this is not possible because of local laws or other impediments, institutions are required to report the fact to their respective regulatory authorities. While there is no direct explicit prohibition against establishing or operating a shell bank, licensing requirements for banks would in practice exclude a bank or other institution with no physical address from gaining a licence to operate. Financial institutions are not required to satisfy themselves that a respondent financial institution in a foreign country does not permit its accounts to be used by shell banks.

20. The HKMA and the SFC have a wide range of enforcement and sanction powers, though the sanctions available with respect to the insurance sector are limited in their scope and do not lend themselves readily to address the wide range of deficiencies that may be identified. In addition, the fit and proper test for insurance institutions applies to chief executives and managing directors but does not apply to other senior management. The current supervision and sanction system for financial institutions does not apply to remittance agents, money lenders, money changers, credit unions, the post office and financial leasing companies.

⁵ This has been addressed in the revised guidance for banks which came into force on 16 May 2008 (after the period of time considered by this evaluation).

21. Since June 2000, all remittance agents and money changers have been required under OSCO to register with the JFIU within one month of commencing business. The authorities have been taking a robust line in dealing with the RAMC sector, pursuing investigations and prosecutions for unregistered activities and failure to keep records and actively engaging the industry in an outreach programme. That said, the provisions within OSCO that bring the remittance sector into the broader AML/CFT regime are quite basic in relation to the overall preventative measures, and do not provide for an oversight regime to access remitters' premises and to check compliance.

4. Preventive Measures – Designated Non-Financial Businesses and Professions

22. All categories of designated non-financial businesses and professions (DNFBPs) as defined by the FATF, except land-based casinos, are found in Hong Kong. In addition, although the operation of casinos is illegal within the jurisdiction, Hong Kong is the home port for several cruise ships offering cruises into international waters principally to provide casino operations. To date, only limited steps have been taken by the authorities to bring any of the categories of DNFBPs into the AML/CFT legal framework with respect to CDD and related obligations. However, a number of professional codes of ethics and standards have some relevance to AML/CFT measures. With the exception of the provisions governing estate agents, which have statutory backing, these are however only in the nature of guidance because they are not underpinned by an explicit and enforceable AML obligation.

23. DNFBPs are subject to the same obligations for reporting suspicious transactions, with associated protection from civil or criminal liability when complying with the reporting obligation, as financial institutions. There is a very low level of reporting by some DNFBPs and complete lack of reporting from others. With the limited exception of the estate agency profession, there are no formal structures in place to monitor AML/CFT compliance within the DNFBP sectors. Some professional associations are however actively involved in raising awareness and encouraging appropriate practices to make their professions resistant to ML and TF. Hong Kong authorities have undertaken significant outreach to the DNFBP sectors to prepare them for eventual incorporation within the legal framework for AML/CFT. In addition, the authorities advise that they have considered applying a greater range of AML/CFT obligations to non-financial businesses and professions (other than DNFBPs) that are at risk of being misused for ML or TF.

5. Legal Persons and Arrangements & Non-Profit Organisations

24. Hong Kong adopts a four-pronged approach to prevent the unlawful use of legal persons and legal arrangements for ML and TF, namely: (a) central registration; (b) investigatory and other powers of law enforcement and financial regulatory authorities; (c) AML/CFT compliance monitoring of financial institutions; and (d) statutory disclosure obligations. These measures are not however adequate to ensure that there is sufficient, accurate and timely information held on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities. Information on the companies register pertains only to legal ownership/control (as opposed to beneficial ownership), is not verified and is not necessarily reliable. Corporate and nominee directors are permitted, which further obscures beneficial ownership and control information. Share warrants to bearer can also be issued in Hong Kong and some additional specific measures are required to ensure that they are not misused for money laundering⁶.

⁶ The Companies Registry is currently assisting in a rewrite of the *Companies Ordinance* in which amendments to the provisions permitting corporate directors and share warrants to bearer will be considered. In addition, the implementation by mid-2008 of new incorporation forms for locally incorporated companies which require provision of company particulars, including details of the directors and secretaries, may help reduce the occurrence of shelf companies.

25. As with many common law jurisdictions, trusts are a long-standing and popular part of the legal and economic landscape. Providers of trust services are not subject to or monitored for AML/CFT obligations. Hong Kong does not have a registry of trusts and it is not known how many trusts have been created in Hong Kong nor how many trustees there are. Some information on trusts is held by government agencies and financial institutions. While powers of investigative agencies to gain information are strong and broad, the fact that most trusts do not come to the attention of authorities and the absence of record-keeping or reporting requirements on trusts makes identifying the trusts or the existence of the trust difficult. Most importantly, there are no requirements that will ensure trust beneficial ownership information would be available to competent authorities on a timely basis.

26. Reviews conducted by Hong Kong authorities of its non-profit sector in 2005 and again in 2006 concluded that there was no particular area of risk in the sector. The reviews also concluded that the present measures to minimise the risk of misuse of non-profit organisations (NPOs) for TF are effective and commensurate with the present risk level of the sector. The NPO sector in Hong Kong is highly diverse and the organisations within the sector vary greatly in size and structure. The exact size and financial scope of the NPO sector is not known, though steps have been taken recently to address this. There is no supervisory authority designated to supervise all NPOs and no requirement for NPOs to register as NPOs, though most NPOs apply for tax-exempt status with the Inland Revenue Department. Requirements to identify persons who own, control or direct the activities of NPOs vary depending on the legal form of the NPO and, for NPOs established as companies (the majority of NPOs), are incomplete. Only NPOs established as companies are required to maintain documents for at least five years. Authorities have recently begun to conduct outreach to this sector, establishing a government/NPO sector focus group in mid-2006 to exchange views on the prevention of TF in the sector and issued advisory guidelines in July 2007 to the sector, but it is too early to fully judge the effectiveness of these efforts.

6. National and International Co-operation

27. Hong Kong does not have a central AML/CFT policy committee and does not have a central AML/CFT strategy as such⁷. Instead, it relies on close working relations between the different policy and regulatory agencies tasked with relevant responsibilities. Staff of relevant competent authorities are clearly involved in co-operative efforts, with a good understanding of each other's role. Joint agency meetings and forums have produced useful guidance and effective operations across all sectors; policy, enforcement and regulatory. On a strategic level however, changes to the AML/CFT system appear to be reactive and there has been a reluctance to elevate matters to the Legislative Council where amendments to ordinances are required.

28. Hong Kong has implemented the provisions of the *Vienna* and *Palermo* Conventions but shortcomings exist in implementation of the *Terrorist Financing Convention* with respect to the TF offence and the freezing obligations. Shortcomings also exist in implementation of the relevant United Nations Security Council Resolutions, as noted previously.

29. The *Mutual Legal Assistance in Criminal Matters Ordinance* offers a wide range of assistance and is generally satisfactory. The power vested in the Central People's Government (of the PRC) to direct refusal of a mutual legal assistance request is potentially of concern, however it is sparingly exercised. The absence of a mechanism enabling Hong Kong to render comprehensive assistance to (and seek assistance from) the PRC and Macao presents a notable gap in an otherwise sound mutual legal assistance regime.

⁷ Since the evaluation, a central co-ordinating committee on AML/CFT, chaired by the Financial Secretary, has been established.

Mutual legal assistance requests are rarely made by Hong Kong authorities for the purpose of proceeds recovery. On the TF front, due to the requirement of dual criminality, gaps in Hong Kong's domestic offences may have an impact on the extent and effectiveness of its capacity to assist others, though this has not presented a problem to date. Hong Kong does not appear to have considered establishing an asset recovery fund, though it does share confiscated assets with other countries from time to time.

30. Hong Kong has an extradition regime that is uncomplicated and not subject to unreasonable grounds for refusal. The discretion to refuse extradition of PRC nationals has, to date, never been exercised. In practice, extradition requests are actioned and concluded expeditiously. As with other forms of mutual legal assistance, however, it is the absence of a mechanism enabling Hong Kong to extradite to (and seek extradition from) other parts of the PRC, that presents the most significant deficit in Hong Kong's extradition arrangements. Due to limitations in the TF offence and the requirement for dual criminality, in order to render extradition in a comprehensive range of TF cases, Hong Kong should address the deficiencies noted previously with respect to the TF offence.

31. Outside the sphere of formal mutual legal assistance and extradition, Hong Kong authorities (enforcement and regulatory) provide a wide range of international co-operation to their foreign counterparts and have clear and effective gateways to facilitate the prompt and constructive exchange of information, both spontaneous and upon request. These arrangements appear to be working well.

7. Resources and Statistics

32. Hong Kong has generally dedicated appropriate financial, human, and technical resources to the various areas of its AML/CFT regime though increased resources in a few areas could lead to increased results. All competent authorities are required to maintain high professional standards, including standards concerning confidentiality, and receive adequate AML/CFT training.

33. Hong Kong generally maintains comprehensive statistics, enabling it to assess the effectiveness of its AML/CFT measures, though it does not conduct a regular review of its AML/CFT regime.

Table 1: Ratings of Compliance with the FATF Recommendations

The ratings of compliance vis-à-vis the FATF Recommendations are made according to the four levels of compliance mentioned in the 2004 Methodology (Compliant (C), Largely Compliant (LC), Partially Compliant (PC), Non-Compliant (NC)), or, in exceptional cases, may be marked as Not Applicable (N/A).

Recommendations	Rating	Summary of Factors Underlying Rating ⁸
Legal systems		
1 – ML offence	LC	<ul style="list-style-type: none"> The predicate offences do not adequately cover one of the 20 designated categories of offences, specifically; environmental crimes.
2 – ML offence – mental element and corporate liability	C	<ul style="list-style-type: none"> This Recommendation is fully observed.
3 – Confiscation and provisional measures	PC	<ul style="list-style-type: none"> OSCO restraint and forfeiture is limited to cases where benefits exceed HK\$100 000. Confiscation powers under OSCO are not available for all predicate offences. No mechanisms exist for confiscation of the proceeds of TF. Powers to confiscate instrumentalities do not extend to property that does not come into the possession of a court or police or customs agencies. Effectiveness: Given the risk of money being laundered in Hong Kong (including the proceeds of foreign predicate offences), the number of restraint and confiscation applications made each year is low.
Preventive measures		
4 – Secrecy laws	C	<ul style="list-style-type: none"> This Recommendation is fully observed.
5 – Customer due diligence	PC	<ul style="list-style-type: none"> Key CDD obligations are not set out in law or regulation. Only basic CDD obligations are in place for money remitters and money exchange companies and, due to the absence of a supervisor for these entities, it is not possible to determine the extent of implementation of the existing CDD obligations. The threshold for CDD on occasional customers in the banking sector (other than in relation to remittances and money changing) is not clearly specified. Pending implementation of the new HKMA Guidelines, there are no obligations on banks to obtain information on the purpose and nature of the account. Scope limitation: no formal assessment has been undertaken to justify exclusion of money lenders, credit unions, the post office and financial leasing companies from CDD requirements.
6 – Politically exposed persons	PC	<ul style="list-style-type: none"> The banking and insurance guidelines do not specify explicitly that senior management approval is required to continue a business relationship with a customer subsequently discovered to be a PEP.

⁸ These factors are only required to be set out when the rating is less than Compliant.

Recommendations	Rating	Summary of Factors Underlying Rating ⁸
		<ul style="list-style-type: none"> • There are no enforceable provisions regarding the identification and verification of PEPs for remittance agents and money changers. • Scope limitation: no formal assessment has been undertaken to justify exclusion of money lenders, credit unions, the post office and financial leasing companies from CDD requirements.
7 – Correspondent banking	C	<ul style="list-style-type: none"> • This Recommendation is fully observed.
8 – New technologies & non face-to-face business	LC	<ul style="list-style-type: none"> • Remittance agents are not required to have policies in place or take measures to prevent the misuse of technological developments in ML and TF schemes. • There is no requirement for remittance agents and money changers (or for AIs undertaking remittance transactions for non-account holders) to verify a customer's identity or to take alternative measures when conducting non-face-to-face transactions. • Scope limitation: no formal assessment has been undertaken to justify exclusion of money lenders, credit unions, the post office and financial leasing companies from CDD requirements.
9 – Third parties and introducers	PC	<ul style="list-style-type: none"> • In the banking and securities sectors, reliance may be placed on introducers who are not regulated for AML/CFT purposes. • Financial institutions may rely on intermediaries incorporated in or operating from "equivalent" jurisdictions but the list of equivalent jurisdictions is not derived from an objective, qualitative assessment. • Scope limitation: no formal assessment has been undertaken to justify exclusion of money lenders, credit unions, the post office and financial leasing companies from the preventive measures.
10 – Record keeping	PC	<ul style="list-style-type: none"> • Only general record-keeping requirements are embedded in law or regulation. • In the securities sector the obligation to maintain identification records, account files and business correspondence for a minimum of five years is recommended but not mandatory. • The record keeping requirements for remittance agents are incomplete: records must only be kept for transactions of HK\$8 000 or more and there is no requirement that remittance agents or money changers verify data obtained and kept for non-face-to-face transactions. • The level of implementation of record keeping requirements by remittance agents and money changers cannot be determined. • Competent authorities may only demand that remittance agents and money changers provide them with records and information where they have a reasonable suspicion that an offence has been committed and this may limit the timely provision of information to competent authorities by remittance agents. • Scope limitation: no formal assessment has been undertaken to justify exclusion of money lenders, credit unions, the post office and financial leasing companies from the preventive measures and corresponding regulatory regime.

Recommendations	Rating	Summary of Factors Underlying Rating ⁸
11 – Unusual transactions	PC	<ul style="list-style-type: none"> • Banking institutions are not currently required to record in writing their findings and analysis of the background and purpose of complex, unusual large transactions or unusual patterns of transactions that have no apparent or visible economic or lawful purpose. • There are no requirements for remittance agents and money changers to pay special attention to complex, unusual large transactions or unusual patterns of transactions that have no apparent or visible economic or lawful purpose. • Scope limitation: no formal assessment has been undertaken to justify exclusion of money lenders, credit unions, the post office and financial leasing companies from the preventive measures.
12 – DNFBPs – R.5, 6, 8-11	NC	<ul style="list-style-type: none"> • With very limited exceptions, no relevant CDD or other obligations (as required under R.5, 6 and 8-11) have been imposed on any of the DNFBP sectors.
13 – Suspicious transaction reporting	LC	<ul style="list-style-type: none"> • Some minor deficiencies in Hong Kong's list of predicate offences (re environmental crime) impact on the scope of the suspicious transaction reporting requirement. • The requirement to report transactions suspected of being related to terrorism only arises where there is a link to terrorist acts, and not where the finances are for a terrorist organisation or individual terrorist in the absence of a link to a terrorist act.
14 – Protection & no tipping-off	LC	<ul style="list-style-type: none"> • The prohibition on tipping-off does not apply in all cases where an STR is being considered, but has not yet been submitted to the JFIU.
15 – Internal controls, compliance & audit	LC	<ul style="list-style-type: none"> • There are no requirements for remittance agents, money changers and money lenders to have internal procedures, policies and controls or to have employee training and screening. • Scope limitation: no formal assessment has been undertaken to justify exclusion of money lenders, credit unions, the post office and financial leasing companies from the preventive measures.
16 – DNFBPs – R.13-15 & 21	NC	<ul style="list-style-type: none"> • Some deficiencies in Hong Kong's list of predicate offences (re environmental crimes) impact on the scope of the suspicious transaction reporting requirement. • The requirement to report transactions suspected of being related to terrorism only arises where there is a link to terrorist acts, and not where the financing is for a terrorist organisation or individual terrorist in the absence of a link to a terrorist act. • The prohibition on tipping-off does not apply in all cases where an STR is being considered, but has not yet been submitted to the JFIU. • There are serious concerns about the effectiveness of the reporting system as most DNFBPs rarely submit reports. • DNFBPs are not obliged to have compliance officers or internal control programmes. • DNFBPs are not required to pay special attention to transactions with countries which do not or do not adequately implement the FATF Recommendations.
17 – Sanctions	PC	<ul style="list-style-type: none"> • Sanctions available with respect to the insurance sector are limited

Recommendations	Rating	Summary of Factors Underlying Rating ⁸
		<p>in their scope and do not lend themselves readily to address the wide range of deficiencies that may be identified.</p> <ul style="list-style-type: none"> • Only criminal sanctions are available with respect to remittance and money changing businesses, and no measures are available to address less serious deficiencies. • Scope limitation: no formal assessment has been undertaken to justify exclusion of money lenders, credit unions, the post office and financial leasing companies from the preventive measures and corresponding regulatory regime. • For institutions regulated by the HKMA, the range of sanctions available does not include the power to impose financial sanctions.
18 – Shell banks	LC	<ul style="list-style-type: none"> • Financial institutions are not required to satisfy themselves that a respondent financial institution in a foreign country does not permit its accounts to be used by shell banks.
19 – Other forms of reporting	C	<ul style="list-style-type: none"> • This Recommendation is fully observed.
20 – Other NFBP & secure transaction techniques	LC	<ul style="list-style-type: none"> • No evidence exists of adequate consideration being paid to applying Recommendations 5, 6, 8-11, 15, 17 and 21 to non-financial businesses and professions (other than DNFBPs) that are at risk of being misused for money laundering or terrorist financing.
21 – Special attention for higher risk countries	LC	<ul style="list-style-type: none"> • There are no requirements for remittance agents or money changers to give special attention to business relationships and transactions with persons from or in countries which do not or insufficiently apply the <i>FATF Recommendations</i>. • Scope limitation: no formal assessment has been undertaken to justify exclusion of money lenders, credit unions, the post office and financial leasing companies from the preventive measures.
22 – Foreign branches & subsidiaries	LC	<ul style="list-style-type: none"> • There are no requirements for remittance agents or money changers to ensure their foreign branches and subsidiaries observe AML/CFT measures consistent with the requirements in Hong Kong and no requirements for the foreign branches and subsidiaries to notify the home supervisor when they are unable to do so.
23 – Regulation, supervision and monitoring	LC	<ul style="list-style-type: none"> • The fit and proper test for insurance institutions applies to chief executives and managing directors but not to senior management. • Remittance 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. • Scope limitation: no formal assessment has been undertaken to justify exclusion of money lenders, credit unions, the post office and financial leasing companies from the preventive measures and corresponding regulatory regime.
24 – DNFBP: regulation, supervision and monitoring	NC	<ul style="list-style-type: none"> • Except for estate agents, there are no designated competent authorities or formal structures in place to monitor DNFBPs' compliance with AML/CFT obligations. • With very limited exceptions, the only sanctions applicable to DNFBPs arise under the criminal law for failure to file STRs.
25 – Guidelines & Feedback	C	<ul style="list-style-type: none"> • This Recommendation is fully observed.

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Institutional and other measures		
26 – The FIU	C	<ul style="list-style-type: none"> This Recommendation is fully observed.
27 – Law enforcement authorities	C	<ul style="list-style-type: none"> This Recommendation is fully observed.
28 – Powers of competent authorities	C	<ul style="list-style-type: none"> This Recommendation is fully observed.
29 – Supervisors	PC	<ul style="list-style-type: none"> The legal authority of the OCI routinely to monitor for AML/CFT compliance and to apply sanctions is limited. There are no powers to permit routine monitoring of remittance and money changing businesses. Only police powers are available to require production of or access to records, documents or information of the remittance agents. Only criminal sanctions are available for individuals running remittance services and these criminal sanctions are not proportionate to the offences, nor do they apply to all AML/CFT requirements. Scope limitation: no formal assessment has been undertaken to justify exclusion of money lenders, credit unions, the post office and financial leasing companies from the preventive measures and corresponding regulatory regime.
30 – Resources, integrity and training	LC	<ul style="list-style-type: none"> There is a need for greater training and awareness-raising to be provided to relevant agencies to address the low number of confiscations relating to ML prosecutions. The number of requests made for mutual legal assistance, particularly for recovery of proceeds of crime, is low, and additional outreach to relevant agencies is required to address this.
31 – National co-operation	LC	<ul style="list-style-type: none"> Effectiveness concern: The mechanisms to co-operate and co-ordinate domestically concerning development and implementation of policies and activities to combat money laundering and terrorist financing are impacted by some reluctance to elevate matters to the Legislative Council where amendments to ordinances are required, and the fact that developments to the AML/CFT system appear to be reactive rather than proactive.
32 – Statistics	LC	<ul style="list-style-type: none"> Hong Kong does not review the effectiveness of its system for combating money laundering and terrorist financing on a regular basis.
33 – Legal persons – beneficial owners	PC	<ul style="list-style-type: none"> Measures are not adequate to ensure that there is sufficient, accurate and timely information held on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities. Information on the companies register pertains only to legal ownership/control (as opposed to beneficial ownership), is not verified and is not necessarily reliable. Corporate and nominee directors are permitted, which further obscures beneficial ownership and control information There are only limited measures in place to ensure that share warrants to bearer, which may be issued by companies incorporated in Hong Kong, are not misused for money laundering.

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34 – Legal arrangements – beneficial owners	PC	<ul style="list-style-type: none"> While the investigative powers are generally sound, there are not adequate measures in place to ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal arrangements that can be obtained or accessed in a timely fashion by competent authorities. Providers of trust services, other than those which are financial institutions, are not subject to or monitored for AML/CFT obligations.
International Co-operation		
35 – Conventions	LC	<ul style="list-style-type: none"> Significant shortcomings exist in implementation of the <i>Terrorist Financing Convention</i> (in particular articles 2, 8 and 18): the TF offence does not extend to ‘funds’ as broadly defined by the Convention; the definition of ‘terrorist act’ does not extend to acts or threats directed at international organisations; the civil ‘protest’ exemptions to certain classes of ‘terrorist acts’ are of potentially broad application; there is no current capacity to effect forfeiture of funds used or allocated for the purpose of committing terrorist offences; and not all customer due diligence requirements have been implemented.
36 – Mutual legal assistance (MLA)	LC	<ul style="list-style-type: none"> Only limited assistance entailing coercive measures is available to “other parts of the People’s Republic of China”, such as Macao and Mainland China, which would be Hong Kong’s most important partners on cross-border crimes. As dual criminality is required for mutual legal assistance, the limitations in the TF offence may have an impact on the extent and effectiveness of mutual legal assistance provided by Hong Kong for TF matters.
37 – Dual criminality	C	<ul style="list-style-type: none"> This Recommendation is fully observed.
38 – MLA on confiscation and freezing	LC	<ul style="list-style-type: none"> Only limited proceeds recovery related assistance is available to “other parts of the People’s Republic of China”, such as Macau and Mainland China for investigations and prosecutions of drug trafficking offences punishable by at least two years’ imprisonment. The mutual legal assistance provisions are seldom used by Hong Kong authorities for the purpose of asset recovery. Insufficient information is available to demonstrate that authorities have considered establishing an asset recovery fund.
39 – Extradition	LC	<ul style="list-style-type: none"> It is not possible to extradite persons to other parts of the PRC, such as Mainland China and Macao.
40 – Other forms of co-operation	C	<ul style="list-style-type: none"> This Recommendation is fully observed.
Nine Special Recommendations		
SR.I – Implement UN instruments	PC	<ul style="list-style-type: none"> Significant shortcomings exist in implementation of the <i>Terrorist Financing Convention</i> (in particular articles 2, 8 and 18): the TF offence does not extend to ‘funds’ as broadly defined by the Convention; the definition of ‘terrorist act’ does not extend to acts or threats directed at international organisations; the ‘civil protest’ exemptions to certain classes of ‘terrorist acts’ are of potentially broad application; there is no current capacity to effect forfeiture of funds used or allocated for the purpose of committing terrorist offences; and not all customer due diligence requirements have

Recommendations	Rating	Summary of Factors Underlying Rating ⁸
		<p>been implemented.</p> <ul style="list-style-type: none"> • S/RES/1373(2001) has not been fully implemented and shortcomings exist in relation to implementation of S/RES/1267(1999); Hong Kong lacks the capacity to implement express freezes on terrorist property and has no capacity to forfeit “funds used or allocated for the purpose of committing” terrorist offences other than those associated with Al Qaeda and the Taliban.
SR.II – Criminalise TF	PC	<ul style="list-style-type: none"> • The TF offence does not encompass provision/collection of assets other than “funds”. • The TF offence under UNATMO does not cover provision/collection for an individual terrorist or terrorist organisation and the offence under UNSAR extends only to those individuals and entities designated by the 1267 Committee. • Terrorist acts as defined in UNATMO do not extend to intended coercion of an international organisation. • The ‘civil protest’ exemptions to certain classes of terrorist acts as defined in UNATMO are potentially of broad application.
SR.III – Freeze and confiscate terrorist assets	PC	<ul style="list-style-type: none"> • Obligations under S/RES/1267(1999) with respect to assets under the direct control of designated entities have not been implemented. • The freezing requirements of S/RES/1373(2001) have not been implemented. • Hong Kong does not have a system for examining and giving effect to actions initiated under freezing mechanisms of other jurisdictions. • There are no provisions concerning jointly held property or property derived from funds or assets owned or controlled by designated entities. • Guidance is not provided to institutions and other natural or legal persons concerning obligations under freezing mechanisms. • There are no mechanisms enabling challenges to freezing actions or enabling access to frozen funds or assets. • There are no provisions with respect to confiscation of funds or other assets of designated entities.
SR.IV – Suspicious transaction reporting	LC	<ul style="list-style-type: none"> • The requirement to report transactions suspected of being related to terrorism only arises where there is a link to terrorist acts, and not where the finances are for a terrorist organisation or individual terrorist in the absence of a link to a terrorist act. • The only reports submitted to date where terrorist financing is suspected relate to potential matches with entities designated on lists.
SR.V – International co-operation	LC	<ul style="list-style-type: none"> • Only limited assistance entailing coercive measures is available to Macao and the PRC and it is not possible to extradite persons between Mainland China, Macao and Hong Kong. • As dual criminality is required, the limitations in the TF offence may have an impact on the extent and effectiveness of mutual legal assistance and extradition provided by Hong Kong for TF matters.
SR.VI – AML requirements for money/value transfer services	PC	<ul style="list-style-type: none"> • There is no system for monitoring remittance services and ensuring they comply with the FATF Recommendations: the only oversight is by use of law enforcement powers. • Only criminal sanctions are available and these are not effective,

Recommendations	Rating	Summary of Factors Underlying Rating ⁸
		<p>proportionate and dissuasive.</p> <ul style="list-style-type: none"> • A broad range of deficiencies identified under other Recommendations are also relevant to the remittance sector.
SR.VII – Wire transfer rules	PC	<ul style="list-style-type: none"> • For remittances ordered by non-accountholders, institutions are only required to conduct verification of the customer's identity for amounts of HK\$8 000 or more when the remitter appears in person. • There is no requirement for remittance agents or the post office to transmit full originator information in the message or form accompanying the wire transfer. • There is no mechanism for monitoring compliance by remittance agents.
SR.VIII – Non-profit organisations	LC	<ul style="list-style-type: none"> • While a domestic review has recently been completed, and various statistics are kept by relevant authorities, there remain some information gaps in relation to the size and financial scope of the NPO sector in Hong Kong. • Outreach has recently commenced to the NPO sector but it is too early to fully judge effectiveness. • Requirements to identify persons who own, control or direct the activities of NPOs vary depending on the legal form of the NPO and, for NPOs established as companies (the majority of NPOs), are not fully adequate, even allowing for the lower level of risk. • The requirement to maintain documents for at least five years is not met for NPOs other than those established as companies under the CO.
SR.IX – Cross-border Declaration & Disclosure	NC	<ul style="list-style-type: none"> • There is neither a disclosure nor a declaration system for detection, seizure or confiscation of cross-border movement of currency or BNI. • Authorities are not empowered to ask for further information where a false/misleading disclosure/declaration has been made. • There is no offence for making a false/misleading declaration or disclosure and authorities are not empowered to seize or confiscate property resulting from a false/misleading disclosure or declaration. • The only specific authority to seize currency or BNI at the border is in relation to property that is related to drug trafficking. • The Immigration Department is not involved in domestic co-ordination mechanisms in this area. • There appears to be no co-ordination or action taken jointly with Mainland China border authorities in relation to the cross-border movement of currency or BNI. • There are no sanctions in cross-border movement of currency or BNI related to ML or TF other than the TF offence itself. • Limited statistics are maintained on cross-border movement of currency or BNI.