

**IFPHK's Response to the Security Bureau's Consultation
Paper on the Establishment of a Reporting System on the
Physical Cross-Boundary Transportation of Large Quantities
of Currency and Bearer Negotiable Instruments**

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Institute of Financial Planners of Hong Kong (IFPHK) Profile

Background

The IFPHK was established in June 2000 as a non-profit organization for the fast-growing financial industry. It aims to be recognized in the region as the premier professional body representing those financial planners that uphold the highest standards for the benefit of the public.

The IFPHK is the sole licensing body in Hong Kong authorized by Financial Planning Standards Board Limited to grant the much-coveted and internationally-recognized CFP^{CM} Certification and AFPTM Certification to qualified financial planning professionals in Hong Kong and Macau.

It represents more than 6,800 financial planning practitioners in Hong Kong from such diverse professional backgrounds as banking, insurance, independent financial advisory, stockbroking, accounting, and legal services.

Currently there are more than 147,000 CFP certificants in 25 countries/regions; the majority of these professionals are in the U.S., Canada, China, Australia and Japan, with more than 4,800 CFP certificants in Hong Kong.

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IFPHK's interest in this consultation

The most common customer type identified by financial planners is the individual consumer. Other customer types include companies, trusts, partnerships, associations, government bodies and agents. A financial planner's duties include maintaining a close relationship with clients. Since Customer Due Diligence ("CDD") is a crucial part of the Anti-Money Laundering ("AML") and Counter Terrorist Financing ("CTF") framework, changes to CDD requirements have an impact on financial planners.

The IFPHK, as the leading professional body representing the interests of the financial planning industry, will respond to any consultation paper that could impact our members and their clients. The IFPHK has already provided its views on two previous rounds of consultation on the legislative proposal to enhance the Anti-Money Laundering ("AML") Regulatory Regime in respect of the Financial Sectors. In November 2012, the IFPHK submitted its view on (1) the Proposed Guideline on Anti-Money Laundering and Counter-Terrorist Financing and (2) the Proposed Prevention of Money Laundering and Terrorist Financing Guideline Issued by the Securities and Futures Commission for Associated Entities.

In light of the above, the IFPHK has an interest in the Consultation Paper and wishes to express its views on the proposed changes to the AML framework in Hong Kong.

IFPHK's representation

The IFPHK was founded by 30 members (the "Founding Members") in order to raise the standards of financial planners and highlight the importance of sound financial planning advice.

The IFPHK currently has 47 Corporate Members including banks, independent financial advisors, insurance companies, and securities brokerages. With our Corporate Members providing a full spectrum of the client services and products, the IFPHK is well positioned to understand the needs, concerns and aspirations of the financial planning community.

Executive Summary

The Financial Action Task Force (“FATF”) is an inter-governmental body established in 1989. It has developed 40 Recommendations for combating money laundering, the financing of terrorism, and the proliferation of weapons of mass destruction. Hong Kong is a member of the FATF and is obliged to implement the AML/CFT requirements as promulgated by the FATF. In order to ensure a full and effective implementation of its Recommendations at the global level, the FATF monitors members’ performance and compliance by conducting mutual evaluations. In the FATF’s mutual evaluation of 2008, Recommendation 32 (“R32”) was the only area where Hong Kong was still rated “non-compliant”. In fact, Hong Kong is the only FATF member jurisdiction, among 34, which has yet to establish the R32 system.

On 21 July, the Security Bureau launched a three-month public consultation on the establishment of a reporting system on the physical cross-boundary transportation of large quantities of currency and bearer negotiable instruments (CBNIs). The Consultation Paper is an effort to move towards compliance with standards established under Recommendation 32 of the FATF on anti-money laundering (AML) and the counter-financing of terrorism (CFT). The R32 System is one of the measures necessary in such a framework.

The views of the IFPHK in the Consultation Paper are based on three principles:

- Aligning with international best practices
- A risk-based supervision approach
- Balancing cost and benefit

In general, the IFPHK agrees with all the proposals stipulated in the Consultation Paper which include the adoption of a mixed declaration and disclosure system for passengers, the use of an advanced electronic submission system for cargo imports and exports, the level of the designated threshold and exclusion of posting of CBNIs.

While it is urgent and critical to comply with the FATF’s recommendations, there is insufficient evidence to indicate that there is a large amount of cross-border smuggling of CBNIs in Hong Kong. A simple R32 system should be implemented initially. Then, in the long run, after more data is collected and more research conducted to assess the risk of money laundering and terrorism financing through the cross-border smuggling of CBNIs, it may be necessary for the Government to review and enhance the R32 system, which in turn may trigger actions such as the level of the designated threshold becoming lower, etc.

The views expressed in this submission paper are not necessarily summaries of the views taken from the industry, but may have undergone more independent and critical analysis and consideration by the IFPHK as a professional body. As a result, not all the views collected by the IFPHK are recorded in this submission paper and neither have all the views expressed in this submission paper been directly endorsed by those industry representatives or members consulted.

The Security Bureau's Consultation

On 21 July, the Security Bureau launched a three-month public consultation on the establishment of a reporting system on the physical cross-boundary transportation of large quantities of currency and bearer negotiable instruments (CBNIs). The three-month consultation period ended on 20 October 2015.

The Consultation Paper is an effort to move towards compliance with standards established under Recommendation 32 of the Financial Action Task Force (FATF) on anti-money laundering (AML) and the counter-financing of terrorism (CFT). The R32 System is one of the measures necessary in such a framework. The proposals in the Consultation Paper are to enable law enforcement agencies to detect and stop the physical movement of illicit funds across the boundaries of different jurisdictions. At present, Hong Kong is the only FATF member jurisdiction, among 34, which has yet to establish the R32 system. In practice, R32 is the only area where Hong Kong was still rated "non-compliant" in the FATF's last round of Mutual Evaluation, which occurred in 2008.

Under the FATF's definition, "currency" refers to domestic banknotes and coins in circulation as well as foreign currency, whereas "bearer negotiable instruments" include monetary or negotiable instruments in bearer form, such as traveller's cheques, cash cheques, promissory notes and money orders.

According to the Government's proposal, passengers arriving in Hong Kong carrying CBNIs valued at over HK\$120,000 should, when undergoing Customs clearance, use the Red Channel under the prevailing Red and Green Channel System and make a declaration. Those leaving Hong Kong will need to disclose the amount of CBNIs carried when asked by a Customs officer. Persons responsible for the import or export of cargo containing CBNIs above the designated threshold should make an advance declaration through an electronic system, in line with the existing systems for the clearance of cargo. The proposed reporting requirements accompany existing Customs clearance practices, and seek to facilitate compliance by members of the public and minimize disturbance caused in view of the huge volume of passenger and cargo flow into and out of Hong Kong every day.

The R32 system is not and should not be regarded as currency control. Members of the public would still be free to bring or transport any amount of cash into and out of Hong Kong. What they need to do is to report to the authority if the amount is over the designated threshold. As electronic payment is becoming more common with banking and financial service advances, the R32 System should have minimal impact on the average traveller, and cross-boundary trade and business transactions.

The Consultation Paper contained 8 questions, and its chapters were as follows:

1 – Executive Summary

2 – Major Components of an R32 System Recommended by the FATF and Overseas Examples

3 – The Proposed R32 System for Hong Kong

4 – Share Your Views

IFPHK's Submission

Consistent with our previous submissions, our comments are based on the following three principles, namely:

Aligning with international best practices

Globalization and financial market integration have increased rapidly in the past decade. As an international financial centre, Hong Kong is not immune from international financial market and regulatory development. As Ashley Alder, CEO of the Securities and Futures Commission ("SFC"), said in the 3rd Pan-Asian Regulatory Summit: "Because Hong Kong is a host city to international investors and companies, things that happen outside our borders really matter and that's why we have to be involved to shape the agenda"¹. International organizations, such as the G20 and FATF, continue to drive financial services sector reform both globally and at a local level to combat money-laundering activities. The FATF has made a series of recommendations to Hong Kong on the cross-border movement of physical currency. Some of the recommendations include to implement a declaration or disclosure system to detect, seize or confiscate the physical cross-border transportation of CBNIs related to money laundering or terrorist financing, to make it an offence to make a false/misleading declaration or disclosure within this system, etc². Hong Kong is behind the curve in implementing regulatory measures over the physical movement of CBNIs. Our major competitor Singapore implemented such measures back in 2007. As Hong Kong is a member of the FATF, the IFPHK and the industry agree that it is important to align local practices with international standards. Financial institutions should strive to ensure that legitimate financial businesses are not allowed to be used as a conduit for money laundering.

A risk-based supervision approach

The recently enacted Anti-money Laundering Ordinance requires financial institutions (FIs) to take all reasonable measures to ensure that proper safeguards exist to prevent a contravention of any Anti-money Laundering ("AML") requirement and to mitigate Money Laundering/Terrorist Financing ("ML/TF") risks. The AML Guidelines implemented in 2012 also encourage FIs to adopt a risk-based approach ("RBA") towards the implementation of AML requirements, taking into consideration the different risk profiles of companies and clients³. Concerns over the physical movement of CBNIs are not new, and the utmost of which are that serious criminals may be retaining the proceeds of their crimes in cash or through the use of bearer negotiable instruments in connection with their money-laundering activities to avoid detection in the banking system. Internationally, responses to bulk-cash smuggling have made use of the three main approaches to crime control include making it more difficult to act illegally, increasing the risk of getting caught, and reducing the rewards of offending. The approach taken by the FATF in its recommendations is to ensure the effective detection of the cross-border transportation of CBNIs and to use prosecution to deter those who fail to comply with border controls, including the confiscation of the proceeds of crime. Countries are able to comply with Recommendation 32 by adopting a declaration system in which persons are required to proactively submit a truthful declaration to authorities about the amounts of CBNIs they are carrying, or by implementing a disclosure system in which persons are required to make a truthful disclosure to authorities only upon request, or a mixture of the two. The aim of the FATF's approach is to deter those who are seeking to launder the proceeds of crime or to engage in the financing of terrorist activities by increasing the likelihood that CBNIs will be detected at national border crossing points⁴. The IFPHK believes the Government should evaluate the ML/TF risks of particular activities when designing the R32 system.

¹ The 3rd Pan-Asian Regulatory Summit was hosted by Thomson Reuters Accelus on 27 & 28 November 2012.

² Source: Hong Kong Money Service Operators Association

³ As suggested in the Guidelines, FIs should assess the ML/TF risk in order to establish and implement adequate and appropriate AML/CTF systems taking into account factors including products and services offered, types of customers, geographical locations involved.

⁴ Trends & issues in crime and criminal justice no. 402 October 2010, Australian Institute of Criminology

Balancing cost and benefit

According to a KPMG survey, the cost of AML compliance has increased and shows no signs of slowing down in the near future. In 2011, eight percent of respondents predicted an over 50 percent increase in expenditure. In reality, 22 percent of respondents increased their expenditure by over 50 percent in the three-year period from 2011. It is not uncommon for survey respondents to underestimate the increase in AML expenditure. Seventy-eight percent of survey respondents reported increases in their total investment in AML activity, with 74 percent also predicting further increases in AML investment over the next three years. The average rate of increase globally was 53 percent compared to a prediction of 40 percent in 2011⁵.

While it is inevitable additional costs will be incurred with the implementation of the new measures proposed in the Consultation Paper, such costs should be kept at a reasonable level and not be onerous to the industry or society.

Question 1: What are your views on the principles we have adopted in devising Hong Kong's R32 System? What other major factors do you think we should take into account?

In devising Hong Kong's R32 System, the government has made reference to the following major principles:

- (a) the system should meet the international standards recommended by the FATF, and at the same time, take into account domestic circumstances;
- (b) the system should be effective in enabling the physical movement of illicit funds to be detected and the flow of such funds to be traced;
- (c) the system is not and would not have the effect of currency control, would not have the effect of currency control, and would not affect the legitimate flow of funds across boundaries;
- (d) the system should facilitate compliance with the reporting obligations by members of the public and minimize any inconvenience caused to them as a result of compliance; and
- (e) the smooth and efficient operation of our existing control points should not be compromised.

Currency and bearer negotiable instruments (CBNIs) according to the FATF are "currency" and "bearer negotiable instruments" (BNIs). "Currency" is defined by the FATF as banknotes and coins that are in circulation as a medium of exchange, and foreign currency which may be brought into a jurisdiction, whereas BNIs include monetary or negotiable instruments in bearer form, such as traveler's cheques, cash, cheques, promissory notes and money orders, in such form that the titles to these pass upon delivery, or include incomplete but signed instruments with the payee's name omitted.

IFPHK's Response:

We consider the principles adopted in the proposed R32 system reasonable. At present, Hong Kong is the only FATF member jurisdiction, among 34, which has yet to establish the R32 system. The IFPHK recognizes the importance of complying with the FATF recommendations, and a R32 system can provide useful data for both conducting analysis and tracing the flow of illicit funds.

⁵ Global Anti-money Laundering Survey 2014, KPMG

Question 2: Do you have any views for Hong Kong to adopt a mixed system for passengers?

Under the FATF’s requirements, members may meet their obligations under R32 by implementing either a declaration system, a disclosure system, or a mixed system, to detect both the incoming and outgoing transportation of large quantities of CBNIs whether by travellers, through cargo or by post. Under a declaration system, persons are required to report to the designated competent authorities, commonly the customs authorities, proactively. Under a disclosure system, travelers are required to provide the authorities with appropriate information upon request. There is no requirement for travelers to make an upfront written or oral report, but they should give a truthful answer to the competent authorities upon request.

The government proposes adopting a mixed system as follows:

Cross-boundary transportation		Proposed reporting type
Passengers	Outgoing	Disclosure (i.e. to report upon request)
	Incoming	Declaration (i.e. to report proactively if CBNIs carried are above designated thresholds)
Cargo	Outgoing and incoming	

IFPHK’s Response:

The IFPHK agrees with the proposal of adopting the mixed system. The arrangement is similar to the existing customs clearance procedure. As such, the IFPHK thinks that it will be easier to both implement and be understood by the public.

Question 3: What do you think of the proposed arrangement of implementing a declaration system with advance electronic submission of information for importing and exporting cargoes?

Hong Kong has already established an electronic infrastructure for the customs clearance of cargo carried by different modes of transport. The Road Cargo System has been established since 2010 to require the advance electronic submission of information of cargo imported or exported through land boundary control points. In addition, there are further arrangements with airlines and shipping companies on the advance electronic submission of cargo information for customs clearance. As such, it is proposed that an advanced electronic declaration system for both incoming and outgoing cargo consignments be adopted. This means that if incoming or outgoing cargo contains CBNIs exceeding the designated threshold, the person responsible for the said cargo (being the owner of the cargo or his/her agent(s)) will be required to make an advanced declaration to the authority concerned, through an electronic system.

IFPHK’s Response:

The IFPHK recommends that the proposed electronic system be simple and easy to use, and an extension of the existing system already in use by the trading industry.

Question 4: Should the FATF’s recommended threshold of USD/EUR15,000 (equivalent to around HK\$120,000) be adopted as the designated threshold for Hong Kong’s R32 System? Or should a lower/higher threshold be adopted?

The proposed designated threshold of HK\$120,000 was drawn up with reference to the FATF’s recommended threshold of USD/EUR15,000. It is largely comparable to or even more relaxed than the thresholds of many other FATF members. The threshold adopted by Australia is AUD10,000 (around

HK\$60,000), USD10,000 (around HK\$78,000) for the US, EUR10,000 (around HK\$86,000) for the UK, and SGD20,000 (around HK\$116,000) for Singapore.

IFPHK's Response:

The IFPHK agrees with the designated threshold of HK\$120,000 which is benchmarked to the FATF's recommended threshold. However, in the long run, the Government may wish to consider implementing a more stringent threshold to keep up with the standard of other advanced economies.

Question 5: For declarations, should we follow the commonly adopted practice of requiring only those transporting CBNIs above the designated threshold to report? Or should all passengers/persons responsible for cargo be required to declare, regardless of the amount of CBNIs they transport?

The proposed threshold will be applicable for declaration by incoming passengers and persons responsible for cross-boundary cargo. Only those bringing or moving CBNIs valued at above the threshold are required to report to the authority concerned. Proactive reporting is not required when the CBNIs carried do not exceed the threshold.

IFPHK's Response:

Initially, the system should only require passengers transporting CBNIs above the designated threshold to report. However, with more research and data, the Government may wish to raise the standard by requiring all passengers or persons responsible for cargo to declare regardless of the amount of CBNIs they transport.

Question 6: Do you think that Hong Kong's R32 system should or should not include specific items such as casino tokens and bearer share certificates?

In line with the FATF's definition of CBNIs, the Government does not intend to require the reporting of the movement of gold and other precious metals and stones. The Government would like to obtain the public views of what other items should be included in the definition of CBNIs.

IFPHK's Response:

The IFPHK has no further suggestions on the definition of CBNIs. Items like casino tokens and bearer share certificates may be included into the R32 system after conducting more research on the ML/TF risks of these items. The IFPHK, however, would like to highlight the risks of money laundering associated with computer chipped cards. Stored value cards (SVC) are now widely used for retail and other purchases, and the limits of value that they can hold are increasing substantially. In the United States, there is some evidence of organized crime groups making use of SVCs to transport funds across national borders⁶. However, it is recognized internationally that there are practical difficulties in regulating SVCs. More research should be done to identify ML/TF trends and, if needed, expand the definition of CBNIs in the R32 system.

⁶ Trends & issues in crime and criminal justice no. 402 October 2010, Australian Institute of Criminology

Question 7: Do you think that Hong Kong should not regulate the posting of CBNIs via the mail system at this stage?

Among the FATF's members, there are divergent approaches regarding whether and how CBNIs are regulated by post.

Country	Approach towards posting of CBNIs
United States	Senders of CBNIs through mail above their respective designated thresholds are required to file declaration forms to the authorities before posting; recipients of CBNIs through mail are also required to file declaration forms to the authorities within a specified period upon receipt.
France	Sending of currency (but not BNIs) by mail is simply prohibited.
Australia	There are reporting requirements for currency (but not BNIs) sent by mail.

In light of the huge volume of international mail, and taking into account the diversity of the modes of regulation worldwide, it is proposed not to regulate the posting of CBNIs via the mail system in Hong Kong at this stage.

IFPHK's Response:

In view of the huge volume⁷ and the potential impact to society, the IFPHK agrees that the posting of CBNIs should not be regulated at this stage. However, in 2010, the FATF reported a case involving over US\$200,000 cash that was discovered in an express outbound mail courier shipment destined for a business in a foreign country of concern. The business and its owner located in the destination country were ultimately identified as members of a known and designated Middle Eastern terrorist organization⁸. As such, the IFPHK thinks that more research should be conducted to assess the ML/TF risk of the posting of CBNIs via the mail system in order to determine whether it warrants regulation in Hong Kong.

Question 8: Do you have any suggestions on how we could enhance the publicity for the implementation of the R32 System so that members of the public and relevant practitioners could be well informed?

The initial publicity plan includes the production of Public Announcements, reminders at the control points, reaching out to the transport trade, etc.

IFPHK's Response:

It is important to emphasize that it is lawful to carry CBNIs above the designated threshold as long as they are reported to the authority. The publicity program should stress that those who fail to comply with the declaration requirements are liable to enforcement actions.

⁷ In the 2014-15 financial year, outbound postal mail from Hong Kong totaled 149.3 million items and inbound postal mail totaled 25.3 million items.

⁸ Trends & issues in crime and criminal justice no. 402 October 2010, Australian Institute of Criminology