IFPHK's Response to the Consultation Paper Issued by the Securities and Futures Commission 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

November 2011

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Profile of IFPHK

Background

IFPHK was established in June 2000 as a non-profit organization for the rapidly expanding finance industry. Its aim is to be recognized as the region's leading professional body representing financial planners who uphold the highest standards of professionalism for the benefit of the public.

The Institute is the sole licensing body authorized by Financial Planning Standards Board Limited to grant the much-coveted and internationally-recognized CFP^CM certification and AFP^TM certification to qualified financial planning professionals in Hong Kong and Macau.

We represent more than 10,000 financial planning practitioners from a broad base of professional backgrounds including banking, insurance, independent financial advisory, stock broking, accounting and legal services.

Currently there are more than 133,000 CFP certificants in 24 countries/regions. The majority of these professionals are in the U.S., Canada, China, Australia and Japan, with more than 4,200 CFP certificants in Hong Kong.

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IFPHK's interest in this consultation

Hong Kong is a member of the Financial Action Task Force ("FATF"), IFPHK and the industry agrees 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.

The most common customer type identified by financial planners is the individual consumer. Other customer types will 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 will have an impact on financial planners.

IFPHK, as the leading professional body representing the interests of the financial planning industry, will respond to any consultation paper that could impact on our members and their clients. 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 fact, representatives of IFPHK have been invited by the SFC to participate in the soft consultation of the proposals sets out in this Consultation Paper. To continue serving the financial planning community, IFPHK wishes to express its views on the proposed Guidelines as stipulated in the Consultation Paper.

IFPHK representation

IFPHK was founded by 30 members (‘Founding Members’) to raise the standards of financial planners and highlight the importance of sound financial planning.

IFPHK currently has 69 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, IFPHK is well positioned to understand the needs, concerns and aspirations of the financial planning community.

Executive Summary

On 30 September 2011, the SFC issued the "Consultation Paper 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". It then invited comments from the industry and the public on the relevant proposals set out in the Consultation Paper.

Pursuant to the changes to the Financial Action Task Force's ("FATF") recommendations and the comments in the mutual evaluation report on Hong Kong[1], the Government proposed to provide statutory backing to the Anti-money Laundering ("AML") framework in Hong Kong. After two rounds of public consultations and a public hearing, on 29 October 2010 the Hong Kong Government gazetted the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Bill (the "Bill"). The Bill is now being considered by a Bills Committee. Targeted for implementation by April 2012, the Bill includes new legislation for customer due diligence (CDD) and record-keeping requirements for financial institutions (FIs).

All financial planners will have obligations under the enacted Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance ("AMLO"). IFPHK considers that as part of the financial community, financial planners will have an obligation and responsibility to fight against money laundering and terrorist financing. Lessons learned from jurisdictions in the West show that large fines for non-compliance cause significant damage to the reputation of the institution involved. Some major banking groups such as ANZ, UBS, Lloyds TSB and ABN AMRO had to learn in the hard way with fines from US authorities, the largest being $350 million. Banks in Asia have also been targeted by US authorities for trading with undesirable partners. Banco Delta Asia from Macau has been censured for trading with North Korea and Malaysian First East Export Bank has been specifically identified as a subsidiary of Iranian Bank Mellat by the US Department of Treasury[2].

In considering the proposed changes in the Consultation Paper, IFPHK's view is based primarily on the following principles:

- *Risk-based supervisory approach:* To adopt a balanced and common sense approach towards supervision and monitoring of the AML requirements by taking into account the risk profile and business models of different financial sectors. Allow for some flexibility and experience through a 'learning curve' for the industry.
- *Level playing field:* Referring to the UK's experience, barriers to a risk based approach include inconsistency of supervision, uncertainty over supervisory enforcement and a lack of supervisory support[3]. As such, all regulators should join force to ensure there is a level playing field for all sectors in order to ensure consistency as well as to share business intelligence among regulators.
- *Balancing cost and benefits:* It is inevitable that additional costs will be incurred with the implementation of the Guidelines. However, such costs shall be kept at reasonable level and not to be onerous to the industry.

IFPHK supports the SFC in replacing the existing Guidance Note with the proposed Guidelines, which provide a uniform set of requirements to all sectors. Generally, IFPHK supports most of the proposals stipulated in the Consultation Paper, particularly the staff training requirements. IFPHK anticipates that more problems will materialize when it enters the implementation phase. Training

[1] While praising the overall effort on the effort to prevent money laundering, the report recommended a few areas that required improvements. The report highlighted that the requirements in Hong Kong are lack of statutory, existing requirements are predominantly in the form of non-statutory regulatory guidance.
[2] The Asian Banker and Temenos, Identifying Anti-Money Laundering Issues in Chinese Banks.
[3] HM Treasury, Review of the Money Laundering Regulations 2007: the Government response, June 2011

and education could help enhance understanding of the AML concepts and ensure a smooth implementation of the AML requirements.

Despite our support for the proposed Guidelines, IFPHK is concerned over the execution of certain requirements under the Guideline. These include the requirement to verify all persons purporting to act on behalf of customers and the requirement to perform company registry search on all locally incorporated non-listed companies and companies incorporated in jurisdictions that have a public company registry. Although IFPHK agrees with the purpose and rationale behind the proposals, we are concerned that the additional costs incurred in complying with the requirements may be burdensome and disproportionate to the ML risks associated with the FIs and the clients of the FIs. IFPHK is also concerned that FIs will seek rapid compliance by adopting a prescriptive approach in obtaining verification documents without fully understanding the purpose of CDD. This would undermine the good intention of the Guideline in promoting a risk based approach on AML and encouraging the FIs in understanding the general ownership and control of the clients. To this end, IFPHK agrees with the speech by the SFC's CEO Ashley Alder in a conference that "It is important for Hong Kong to work closely with the industry and other regulators to promote solutions which protect investors and underpin stability". Also his statement that "quality regulation results from an interactive process, which is why it is important for an organization like SFC to continue to communicate with a cross section of the market as well as globally".

Beside, format of the Guideline is too lengthy with cross-referencing and important notes in small print. To facilitate and enhance industry awareness of the new requirements, IFPHK suggests the SFC to highlight key areas that are specific to the securities and futures sector in an FAQ.

The SFC Consultation

The enacted Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance (“AMLO”) shall come into effect on 1 April 2011. The purpose of the AMLO is to enhance the Anti-Money Laundering (“AML”) or Counter-Terrorist Financing (“CTF”) regime in Hong Kong with respect to the finance sector so as to meet the requirements set by the Financial Action Task Force (“FATF”). AMLO provides a uniform set of requirements applicable to all financial institutions (“FIs”). The SFC is of the view that generic guidance applicable to all FIs is generally adequate and appropriate to the securities and futures sector. Further guidance will only be needed when dealing with sector-specific examples. As such, the SFC issued a “Consultation Paper 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” (the “Consultation Paper”) on 30 September 2011.

The Consultation Paper offers proposals for a new set of guidelines on anti-money laundering and counter-terrorist financing (the “Guidelines”). The Guidelines will replace the existing Prevention of Money Laundering and Terrorist Financing Guidance Note (“AMLGN”) published by the SFC. The Guidelines seek to provide guidance to the industry relating to the operation of the provisions of Schedule 2 of the AMLO, which shall come in to effect on 1 April 2012.

The key objective of the Guidelines is to assist licensed corporations (“LCs”) in designing and implementing appropriate and effective policies, procedures and controls to meet with the AMLO and other applicable AML or CTF requirements. The Guidelines also include industry-specific examples on suspicious transactions and reporting them to Joint Financial Intelligence Unit (“JFIU”).

The Consultation Paper contains five questions relating to the following topics for the industry and public to provide comments:

1. Person purporting to act on behalf of customers
2. Wire transfers
3. Performance of a company registry search
4. Nominee companies
5. Staff training

IFPHK's Submission

Key Principles
Prior to providing our views on the questions stipulated in the Consultation Paper, we wish to point out that the IFPHK's responses are formed upon the following principles:

Risk based supervision approach
AMLO requires FIs to take all reasonable measures to ensure that proper safeguards exist to prevent a contravention of any AML requirement and to mitigate ML/TF risk. The Guidelines also encourage FIs to adopt a risk based approach ("RBA") towards implementation of AML requirements, taking into consideration different risk profiles of companies and clients[4]. If effectively implemented, the RBA approach will ensure that lower risk clients do not suffer from unduly burdensome procedures and requirements. On the other hand, it will ensure that FIs undertake enhanced due diligence whenever it is required for clients, products and services that pose higher risk.

The ML risks faced by the financial planning industry and other securities related sectors are different from those experienced by the banking sector. As highlighted in FATF's typology report, the risks faced by the securities sector are not in respect of the placement stage of money laundering, but rather in the layering and integration stages. Typical securities sector related laundering schemes often involve a series of transactions that do not match the investor's profile and do not appear designed to provide a return on investment. Reporting of suspicious transactions by the sector remains relatively low, which can be explained by a number of possible factors including a lack of awareness and insufficient sector-specific indicators and case studies[5].

Moreover, the majority of financial planners (with the exception of those in the banking and insurance sector) usually operate on a small scale. Some financial planners just advise or simply "arrange" for their clients to receive the designated services of others. Therefore the risk of money laundering within the financial planning industry is lower compared to other financial sectors. In addition, financial planners will have already performed due diligence on their clients in the Know Your Client ("KYC") procedure which satisfies some of the obligations in the Guideline. In consideration of the lower risk nature of the financial planning industry, IFPHK suggests the SFC adopts a balanced and common sense approach towards supervision and monitoring of the AML requirements by taking into account the risk profile and business models of different financial sectors, and allowing some flexibility and learning curve experience to the industry.

Level playing field
IFPHK would like to reinforce its stance on previous submissions to the two rounds public consultation on the AMLO that the new rules and Guideline shall provide a level playing field for the industry. Whilst IFPHK welcomes the establishment of a uniform set of basic requirements for all sectors, implementation of the Guidelines shall take into consideration of the complexities and business models of different sectors. They should allow for flexibility and cater for differences in the business sector in order to facilitate effective regulatory measures and meaningful enforcement functions. As noted in the review conducted by UK's HM Treasury on the effectiveness of RBA on AML, the barriers to a risk-based approach are inconsistency of supervision, uncertainty of supervisory enforcement and a lack of supervisory support.[6] Thus, IFPHK considers it important to ensure consistency of supervisors in terms of compliance monitoring and enforcement. IFPHK suggests the SFC to maintain and strengthen the coordination between different regulators not only to ensure consistency, but also to share

[4] 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.
[5] FATF, Money Laundering and Terrorist Financing in the Securities Sector, October 2009
[6] HM Treasury, Review of the Money Laundering Regulations 2007: the Government response, June 2011

business intelligence on money laundering news and issues that could help to provide a level playing field across all financial sectors.

Balancing cost and benefit
According a survey by KPMG, cost of AML compliance has risen by an average 45 percent in the last three years, with more than 80 percent of respondents reporting a cost increase over that time. In the Asia Pacific region regulatory enforcement actions have centered on identified deficiencies in the reporting of suspicious activity, which may have led to a greater focus on this area[7]. While it is inevitable additional costs will be incurred with the implementation of the Guidelines, such costs should be kept at reasonable level and not to be onerous to the industry. As seen with the implementation of AML requirements in China, Chinese banks spent a tremendous amount, especially in data management and technology, when complying with the requirements. However, rushed compliance by these banks did not necessarily result in efficient capabilities for fighting money laundering. There is still mis-understanding on the purposes and principles behind the AML requirements[8], which will affect the quality of AML monitoring and suspicious transaction reporting.

Consultation Questions raised in the Consultation Paper

1) Persons purporting to act on behalf of customers

Question 1:

Do you think paras 4.41, 4.4.3 and 4.9.19 together provide sufficient guidance to assist FIs in complying with the requirement of taking reasonable measures to verify the identity of persons purporting to act on behalf of customers? If not, please suggest further examples or alternative measures with reasons.

FIs should identify all persons purporting to act on behalf of customers, take reasonable measures to verify their identity and verify their authority to act on behalf of the customer. For customers that are legal persons of legal arrangements, FIs should be required to verify that any person purporting to act on behalf of the customer is so authorized, and identify and verify the identity of that person. In view of the concern over the broad meaning of "a person purporting to act on behalf of the customer" and the practicality of identifying all these persons, some flexibility has been provided in the Guideline as to what measures would be considered reasonable for verifying the identity of such persons. For example, para 4.9.19 of the proposed Guidelines presently provides further methods in verifying the identities of account signatories, which includes allowing an FI to adopt a streamlined approach in verifying the identities of account signatories based on its risk assessment of the customer and where the customer is an FI or a listed company.

<u>IFPHK's Response</u>

As suggested in the FATF's typology report, sophisticated criminals will try to hide behind business structures and agents to help facilitate money laundering. Therefore, IFPHK agrees that better understanding of the client's ownership and control structure will help FIs to understand the purpose and motivation behind transactions, and thereby enable the institutions to spot suspicious activities related to money laundering. However, the requirement for CDD should be proportionate to the risk because eventually the percentage of individuals who use corporate vehicles and legal arrangements for legitimate purposes will significantly outweigh the percentage that uses them for criminal means.

[7] KPMG, Global Anti-Money Laundering Survey 2011, How banks are facing up to the challenge
[8] The Asian Banker and Temenos, Identifying Anti-Money Laundering Issues in Chinese Banks,

Existing standards on KYC already require FIs to identify clients and beneficial owners including a person on whose behalf the transaction is undertaken. Therefore, any additional requirement requesting FIs to verify the identities of **all** persons purporting to act on behalf of customers and to verify their authority to act may incur considerable costs on the industry. Yet it may not prevent criminals providing false details on beneficial ownership and control structures. As stated in the typology report of FATF, warning signs of money laundering often come not from the owners, but from the nature of their business, the specific transactions they are undertaking and the size and source of funds they are utilizing.

To address the issues of additional costs and new burdens to the industry, IFPHK welcomes the proposal of allowing FIs to apply a streamlined approach on certain types of customers, such as FIs or listed companies, Such a relaxation is set out clearly in para 4.9.19. Nonetheless, the requirements of obtaining evidence of authority to act did create a burden to the industry and IFPHK urges the SFC and other regulators to adopt a common sense approach rather than a checklist approach on its supervision and monitoring of the requirement, by taking into account the risk profile of the FIs and the ML risks of the client in each scenario.

2) Wire transfers

Question 2:

Do you think Chapter 10, particularly para. 10.1, is sufficiently clear as to when the wire transfer provisions do not apply to an LC? If not, what further guidance may be useful in this respect?

The AMLO requires FIs when carrying out wire transfers to verify and record various identification information of the originator of the wire transfer. Definition of a wire transfer is defined under Part 1 of Schedule 2 to the AMLO[9]. SFC acknowledges the industry's comments that LCs would typically only be the originators or recipients or beneficiaries in wire transfer transactions. Therefore, the guidelines include clarification that the wire transfer requirements primarily apply to authorized institutions and money service operators.

IFPHK's Response

Wire transfers occur through and between banks. IFPHK acknowledges that financial planners like other licensed corporations with SFC usually act as the originator or beneficiary or recipient in wire transactions and thus the role of financial planners in a wire transfer is less important than that of a bank. Nonetheless, the financial planning and other securities sectors need to aware of some ML indicators in relation to wire transfer. While cash is generally not accepted by financial planners cheques can sometimes be used to fund an account with an intermediary, or used to directly purchase investment products. Although these cheques are usually drawn from a depository account and occasionally money orders, traveler's cheques and cashier's cheques can be used to complete a transaction. Money launderers can purchase money orders, traveler's cheques, and/or cashier's cheques with cash over a period of time or through a series of transactions in order to avoid threshold currency reporting requirements. These cheques can then be used to purchase investment products, which are then sold or transferred. Another ML indicator relating to cheques is when outgoing cheques to third parties coincide with or are close in time to incoming cheques from other third parties.

[9] A transaction carried out by an institution (the ordering institution) on behalf of a person by electronic means with a view to making an amount of money available to that person or another person (the recipient) at an institution (the beneficiary institution), which may be the ordering institution or another institution, whether or not one or more other institutions (the intermediary institutions) participate in completion of the transfer of the money

Overall, IFPHK believes para 10.1 of the Guidelines sufficiently explains that chapter 10 primarily applies to authorized institutions and money service operators. For easy referencing IFPHK suggests the SFC put the explanation and some of the ML indicators related to check payment in an FAQ.

3) Performance of a company registry search

Question 3:

Do you agree that the benefits of performing a company registry search as an independent effective means of confirming a corporate customer's current status and verifying the names of its directors and shareholders outweigh the costs?

The Guideline contains additional requirements of FIs to perform a company registry search and obtain a full company search report in respect of all locally incorporated non-listed companies and companies incorporated in jurisdictions which have a public company registry as part of the customer due diligence ("CDD") process. Alternatively, FIs may obtain from the customer a certified true copy of a full company search report. The purpose of the requirement is to:

- Confirm that the company is still registered and has not been dissolved, wound up, suspended or struck off;
- Independently identify and verify the names of the directors and shareholders recorded in the company registry in the place of incorporation; and
- Verify the company's registered office address in place of incorporation.

IFPHK's Response

One of the biggest challenges of the current AML system is to identify the beneficial owner or beneficiary of legal persons and arrangements. At present money launderers use legal persons in their schemes because of the difficulty of obtaining beneficial ownership information. However, legal persons are the creation of the authorities and corporate vehicles are a very common business structure around the world[10]. In most case the purpose behind their formation is completely legitimate. Therefore, IFPHK strongly believes that the onus should be on the Government or other related authorities to collect, verify and publish beneficial ownership information. It is contradicting to place heavy burdens on FIs to identify and verify the beneficial ownership of their clients, while permitting some jurisdictions to restrict the amount of information available in the public domain.

Whilst IFPHK agrees that **company search can be used to ascertain the existence of a legal person**, IFPHK is uncertain about its overall effectiveness in CDD. Although company search is useful in verifying legal ownership the true beneficial owner may still be hidden, especially when ownership chains move into jurisdictions without such registers or public registers that does not provide adequate information. The cost of searching for the ultimate beneficial owners may become burdensome for FIs. With respect to verifying the registered office address, a registered office address may simply be a postal box in the jurisdiction where the company has been formed, which may be serviced by a corporate service agency.

It may not be cost effective for smaller firms to insist on seeking an ultimate beneficial ownership. Such requirements could be used for identifying and managing real areas of risk. As noted above, complex structures are usually set up with a specific purpose e.g. tax administration or joint ventures, and someone within the company should be able to explain the ownership chain. The real money laundering risk associated with corporate vehicles occurs where the company is set up with the purpose of disguising the proceeds of crime from other activities undertaken by its owners. Thus the costs of beneficial ownership CDD, which in many cases far outweighs the

[10] The number of companies on the company register in Hong Kong grew from 710,768 in 2008 to 863,762 in 2010.

benefits, means huge amounts of time and money will be spent in collecting document that, only in rare situations, will lead to any suspicion that the client is involved in money laundering.

Instead of placing a heavy reliance on FIs to identify and verify ultimate ownership, there are certain types of professionals such as those listed below that might share the responsibility on CDD of legal persons with FIs.

Company formation agents
The company formation agent should be required to conduct due diligence on the beneficial owners at the point of formation. They should endeavor to understand the reason for specific incorporation of the company and the business it will conduct and assess the risk of money laundering of the new company.

Legal persons
In order to illustrate that their company structure is set up with legitimate purpose, legal persons should be obliged to hold information about their own beneficial ownership including documentary proof. This beneficial ownership information, along with the documentary proof, should then be submitted to a government authority. The authority should collect and verify beneficial ownership information. Penalties, including banning orders prohibiting control, ownership or management of corporate vehicles for periods of time, should be imposed on those who control and own corporate vehicles who do not keep these details up-to-date.

Government Authority
Beneficial ownership information should at the very least be available to competent authorities in the jurisdiction where the legal person is registered, as well as competent authorities in any jurisdiction where the legal person operates. FIs should be able to access the widest range of information sources at reasonable cost.

IFPHK recognizes that company registry in Hong Kong provides a useful source of information for identifying beneficial ownership or tracing ownership chains at reasonable cost. The use of the company registry is indeed very common in Hong Kong. The number of company searches in 2010 amounted to 3,113,758, which means that each company on the register was searched for 3.6 times[11]. IFPHK agrees that the requirement to perform a company search on **locally incorporated** companies would not add significant cost, However, IFPHK has some concerns to the extent requirements apply to companies incorporated outside of Hong Kong in jurisdictions where they might not have a public register or the public register does not provide adequate information.

IFPHK considers that supervision focus should be placed on identification rather than verification of **all** beneficial ownership. It is more useful for the FIs to understand the general ownership and control of the client, rather than a specific pursuit of the named natural persons, unless there are other warning signs of potential money laundering. This approach is to ensure that FIs would still be required to understand who their client is, but would limit the resource intensive profiling of client ownership chains in those situations where there is some evidence of higher ML risk.

4) Nominee companies

Question 4:

Para. 4.10.6 covers fund distribution activities involving the holding of fund units by nominee companies. Do you think that there are other types of business relationships involving nominee companies controlled by an FI distributor that should also be covered by this provision? If so, please provide details with reasons.

[11] On the basis of 863,762 numbers of companies listed on Hong Kong's company register in 2010.

FI may apply simplified due diligence ("SDD") whereby it is not required to identify and verify the beneficial owners in relation to a customer if the customer is another FI. The SFC recognizes that it is common for the fund distributor to open an account with a fund house or product issuer in the name of a nominee account for holding fund units on behalf of the customers of the fund distributor. To address the fund industry's concerns, the Guideline is drafted such that, subject to certain safeguards, the fund distributor is regarded as the customer of the fund house and not the nominee company. The safeguards include the requirements that the fund distributor is a FI and has conducted CDD on the underlying customers of the fund, and is authorized to operate the account which is in the name of the nominee company pursuant to a contractual document or agreement.

IFPHK's Response

Typology reports of FATF indicated that complex structures with nominee shareholders represent a high risk from money laundering. Nominee accounts present vulnerabilities in the layering and integration stages. A particular risk involves jurisdictions where the formation of a nominee account does not require collecting beneficial ownership information for individuals. Regardless of the risks, there are quite a number of examples where nominee shareholding structures are utilized for legitimate reasons. In the financial planning universe, stocks and shares are held in a discretionary managed portfolio by an investment manager so that the stock can be dealt with on a timely basis. Most nominee shareholders are regulated financial intermediaries and so are already regulated for money laundering compliance[12]. Hence, IFPHK agrees that Financial Planners or other fund distributors can be regarded as a customer of the fund house and the account does not need to be classified as a nominee account.

IFPHK believes all FIs should be able to reasonably rely on other regulated entities and presume that the regulated entity has in place appropriate risk-based CDD procedures. The purpose of promoting reliance is to reduce red tape and the cost of duplicate and unnecessary CDD processes being conducted by multiple parties for the same client and the same transaction. It also helps to reduce widespread copying and retention of copies of identification documents, and solve the practical issues for businesses in managing large volumes of documentation. Given the importance of the CDD reliance, the interaction between product issuers and financial planners (or distributors) in the CDD process and the corresponding record keeping requirements shall be properly addressed and illustrated in an FAQ.

5) Staff training

Question 5:

Do you agree that FIs should implement a clear and well articulated policy for ensuring that relevant staff receive adequate AML/CTF training and monitor its effectiveness?

The Guideline requires FIs to implement policies and procedures to ensure that staff receives adequate and effective training on AML and CTF and FIs should monitor the effective of these policies and procedures.

IFPHK's Response

IFPHK strongly agrees that staff training is an important element of an effective AML system. In this regard FIs must ensure that staff are adequately trained. As highlighted earlier the experience of the Chinese banks told us that capabilities to fight against money laundering do not necessarily arrive with the implementation of new rules. The regulations were the drivers for the implementation of AML operations, but a deeper understanding of the necessity of AML and CTF

[12] Financial Planning Association, The AML/CTF Regime – Preparing for December 12

is more fundamental. In spite of the importance of training in promoting AML, resources are not usually allocated to this area. The AML benchmarking survey conducted by ICAEW found that not all firms[13] provided annual training to their staff, despite the fact they stated that they relied on staff training to make sure that the firm fully complied with regulatory requirements.

Training is crucial for smaller firms who have less resource to invest in an AML compliance system and technology. As such they rely heavily on staffs' logical reasoning and sensitive recognition in reporting suspicious transactions. Staff should be adequately trained with the skills that enable them to stay alert. Since the Guideline requires senior management of FIs to make a judgment on the reasonableness of the beneficial ownership information provided to them, they need to ask themselves whether it is sensible for the beneficial owners, given where they live, their age and their occupation, to be the actual owner of the assets in question. Senior management needs intensive training to equip them with the knowledge and skills to make sensible judgments that meet the requirements. As discussed before, suspicious transaction reporting in the securities sector remains relatively low due to a lack of awareness, insufficient sector-specific indicators and case studies. At present, AML training available in the market is usually generic or more relevant to the banking industry. The SFC could work with the industry to come up with more sector-specific AML training programs and materials. Regulators' support is critical to increase the learning curve of the AML measures within the industry.

In view of the need for AML training, IFPHK strongly supports the inclusion of training requirements in the Guideline. IFPHK considers key success factors of an effective AML training program should include but not limited to the following:

Relevancy: Applicable and relevant training should be provided to all staff. Training should be tailored to the requirements of staff according to their roles and responsibilities. Training should be specific to business lines if there is a difference in risk. Training should ensure all staff understand their role in maintaining an effective AML compliance.

On-going: Training should be provided periodically and at regular intervals. Overview of AML requirements should be included in orientation or induction training for new hires. Ongoing training programs should incorporate the latest developments and changes to regulations.

Practicality: The training should include and give reference to internal policies, procedures and processes so that staff can apply their AML knowledge in their daily routine. The training should include examples involving money laundering and suspicious activity monitoring and reporting. These examples should be tailored for different audiences according to their business lines, roles and responsibilities.

Record keeping: The training programs should be well documented. The records of training, including the training and testing material, training session dates, attendance, etc must be maintained properly.

Other Issues

In addition to the IFPHK's view on the questions stipulated in the Consultation Paper, IFPHK would also like to highlight some other suggestion for the SFC's consideration.

Format of the Guideline

IFPHK believes that a uniform set of requirements for all financial sectors could promote an effective and proportionate approach to the AMLO. However, the Guideline is too lengthy and some explanations and important notes are stated in small font. While it is a licensed persons' responsibility to understand and be conversant with all the requirements under the Guidelines, IFPHK suggests the SFC help the industry by highlighting some key areas that are relevant to the securities and futures sector in an FAQ.

[13] All participants are accounting firm

Conclusion

Global awareness on prevention of money laundering and terrorist financing has increased substantially and expanded outside of banking sector. It is clear that having a robust AML/CTF system in place is not only good for compliance with regulatory requirements, but also to protect an institution's reputation. While traditionally the risks and responsibilities have fallen on banks, the need for effective AML/CTF controls apply equally to securities companies, insurance companies, financial advisors and other financial institutions.

IFPHK endorses the proposal of having a generic AML Guideline for all financial services sectors. We also support the risk based approach ("RBA") on AML and CTF. The RBA gives businesses flexibility in their implementation of the regulations and it helps avoid the prescriptive application of the regulations under which emphasis is placed on discharging requirements rather than the implementation of effective AML practice. RBA should help to minimize costs to business and ensure the regulations are effective and proportionately implemented on a case-by-case basis by reflecting the risk profile of the business. IFPHK would encourage members to fully embrace the risk-based approach to AML and enhance their senior management's accountability for effective AML. On the other hand, IFPHK urges the SFC to adopt a balanced and common sense approach to its supervision roles. Monitoring activities should focus on the higher risk LCs and avoid using a checklist approach on AML compliance.

Although IFPHK supports most of the proposals in the Guidelines particularly the staff training requirements, we are in two minds regarding the execution and implementation of certain requirements, especially on the changes to CDD. Beneficial ownership information available to FIs or in the public domain in some jurisdictions is still incomplete. There is a need to ensure that company and trust beneficial ownership and control information is accessible in a timely, accurate and transparent manner. In practice much of the beneficial ownership and control structure information that may be required is not available through independent channels. This is particularly the case for legal persons registered overseas. The lack of reliable information tends to result in LCs seeking numerous documents, irrespective of the risk present, which is contrary to the RBA that IFPHK advocates. Overall IFPHK regards the requirements as sensible, but we wish the SFC allow the industry some flexibility especially at the beginning of the implementation phase. Like most cases with the introduction of new requirements, problems will arise as companies enter the implementation phase.

Finally, IFPHK appreciates that there was extensive dialogue prior to the introduction of the Guidelines and we were provided with the opportunity to contribute to the development of the Guideline. We hope that this ongoing engagement between the regulatory authorities and the industry continues.