

**ENHANCING ANTI-MONEY LAUNDERING REGULATION OF
DESIGNATED NON-FINANCIAL BUSINESSES AND
PROFESSIONS**

**UNITED NATIONS (ANTI-TERRORISM MEASURES)
ORDINANCE – PROPOSALS FOR AMENDMENTS**

The Law Society's Submissions

1. The Law Society has reviewed the following consultation papers issued by the Financial Services and the Treasury Bureau and the Security Bureau (“FSTB”) in January 2017:
 - (a) Enhancing Anti-Money Laundering Regulation of Designated Non-Financial Businesses and Professions (“DNFBP Consultation Paper”); and
 - (b) United Nations (Anti-Terrorism Measures) Ordinance – Proposals for Amendments (“UNATMO Consultation Paper”).

(A) *DNFBP Consultation Paper – Some Background*

2. The Law Society has reviewed the following Recommendations issued by the Financial Action Task Force (“FATF”):

(a) FATF Recommendation 10 – Customer Due Diligence (“CDD”)

Financial institutions should be required to undertake CDD when:-

- (i) establishing business relations;
- (ii) carrying out occasional transactions: (i) above the applicable designated threshold (USD/EUR 15,000); or (ii) that are wire

transfers in the circumstances covered by the Interpretative Note to Recommendation 16;

- (iii) there is a suspicion of money laundering or terrorist financing; or
- (iv) the financial institution has doubts about the veracity or adequacy of previously obtained customer identification data.

The principle that financial institutions should conduct CDD should be set out in law. Each country may determine how it imposes specific CDD obligations, either through law or enforceable means.

The CDD measures to be taken are as follows:-

- (i) Identifying the customer and verifying that customer's identity using reliable, independent source documents, data or information.
- (ii) Identifying the beneficial owner, and taking reasonable measures to verify the identity of the beneficial owner, such that the financial institution is satisfied that it knows who the beneficial owner is. For legal persons and arrangements this should include financial institutions understanding the ownership and control structure of the customer.
- (iii) Understanding and, as appropriate, obtaining information on the purpose and intended nature of the business relationship.
- (iv) Conducting ongoing due diligence on the business relationship and scrutiny of transactions undertaken throughout the course of that relationship to ensure that the transactions being conducted are consistent with the institution's knowledge of the customer, their business and risk profile, including, where necessary, the source of funds.

(b) FATF Recommendation 11 – record keeping

Financial institutions should be required to maintain, for at least five years, all necessary records on transactions, both domestic and international, to enable them to comply swiftly with information requests from the competent authorities. Such records must be sufficient to permit reconstruction of individual transactions (including the amounts and types of currency involved, if any) so as to provide, if necessary, evidence for prosecution of criminal activity.

Financial institutions should be required to keep all records obtained through CDD measures (e.g. copies or records of official identification documents like passports, identity cards, driving licences or similar documents), account files and business correspondence, including the

results of any analysis undertaken (e.g. inquiries to establish the background and purpose of complex, unusual large transactions), for at least five years after the business relationship is ended, or after the date of the occasional transaction.

Financial institutions should be required by law to maintain records on transactions and information obtained through the CDD measures.

(c) FATF Recommendation 22 – Designated Non-Financial Businesses and Professions (“DNFBP”)

The CDD and record keeping requirements set out in Recommendations 10, 11, 12, 15 and 17 apply to DNFBP including lawyers when they prepare for or carry out transactions for their clients relating to the following activities:-

- (i) buying and selling of real estate;
- (ii) managing of client money, securities or other assets;
- (iii) management of bank, savings or securities accounts;
- (iv) organisation of contributions for the creation, operation or management of companies;
- (v) creation, operation or management of legal persons or arrangements, and buying and selling of business entities.

(d) Legal basis of requirements on financial institutions and DNFBP (“Legal basis”) issued by the FATF

- (i) In Recommendations 10, 11 and 20, the term “law” refers to any legislation issued or approved through a Parliamentary process or other equivalent means provided for under the country’s constitutional framework, which imposes mandatory requirements with sanctions for non-compliance. The sanctions for non-compliance should be effective, proportionate and dissuasive (see Recommendation 35). The notion of law also encompasses judicial decisions that impose relevant requirements, and which are binding and authoritative in all parts of the country.
- (ii) The term “Enforceable means” refers to regulations, guidelines, instructions or other documents or mechanisms that set out enforceable anti-money laundering (“AML”) / counter financing of terrorism (“CFT”) requirements in mandatory language with sanctions for non-compliance, and which are issued or approved by a competent authority. The sanctions for non-compliance should be effective, proportionate and dissuasive (see Recommendation 35).

3. The Legal Practitioners Ordinance (“LPO”) bestows upon the Law Society the very important statutory function of regulating the professional practice of solicitors in the public interest. Section 7 of the LPO sets out the qualification requirements for practising as solicitors. No person shall be qualified to act as a solicitor unless his or her name is on the roll of solicitors; he or she is not suspended from practice and he or she has in force a current practising certificate. The Law Society is the statutory body which is empowered to issue practising certificates under section 6 of the LPO.
4. The Law Society is empowered to issue Practice Directions relating to the professional practice, conduct and discipline of solicitors.
5. Every Member is absolutely bound by, all Practice Directions, rules and regulations from time to time issued by the Law Society and each Member is deemed to have given an undertaking to the Law Society to abide by all such Practice Directions, rules and regulations.
6. Pursuant to its power, the Law Society issued Practice Direction P on 3 December 2007. It is a comprehensive set of AML regulations. This Practice Direction consists of, inter alia:
 - (a) a table of mandatory requirements for law firms on client identification and verification, CDD exercises, record keeping;
 - (b) a summary of the current relevant legislation on money laundering and terrorist financing;
 - (c) basic policies and procedures required of law firms;
 - (d) relevant legal issues on legal professional privilege, client confidentiality, litigation, civil liability and confidentiality agreements;
 - (e) examples of suspicious transaction indicators and risk areas; and
 - (f) suspicious transaction reporting.

Table A and paragraphs 18 to 28 of Practice Direction P set out the mandatory requirements of client identification and verification, CDD, record keeping and staff training.

7. Table A and paragraphs 18 to 28 of Practice Direction P have mandatory effect. Any law firm, solicitor or foreign lawyer practising in Hong Kong who fails to

comply with the mandatory provisions will face disciplinary proceedings. Members are aware that if they do not comply with the provisions in Practice Direction P, they will be exposed to additional risk of being involved in money laundering and terrorist financing activities with severe consequences of criminal prosecution and significant loss of reputation.

8. The Law Society, as a self-regulatory body, is empowered under section 9A of the LPO to refer a breach of Practice Direction P to the Solicitors Disciplinary Tribunal (“Tribunal”) for determination. The DNFBP Consultation Paper fails to recognise the stringent regulatory and disciplinary regime that applies to solicitors and registered foreign lawyers.
9. The Tribunal has wide ranging power under section 10 of the LPO to impose sanctions on solicitors, trainee solicitors, foreign lawyers and unqualified persons employed by law firms. It has statutory powers to order censure, payment of penalty and impose conditions on a solicitor’s practice. The most severe sanction is striking off a solicitor’s name from the roll of solicitors. The Council can deploy Monitoring Accountants to examine the law firm’s accounts and investigate their accounting records and books. The Law Society also has the statutory power to intervene in a law firm’s practice under prescribed statutory circumstances.
10. With the implementation of Practice Direction P, the Law Society has established a legal AML mechanism which is binding, enforceable and authoritative for its Members. Practice Direction P satisfies the FATF Recommendations on CDD and record keeping. Practice Direction P has the effect of law and is enforceable by sanctions which are effective, proportionate and dissuasive. As a matter of substance, Practice Direction P is effective; as a matter of form, it is backed by law and is enforceable. Judicial consideration by the Courts has determined that Practice Direction P is a protocol of good practice. If due consideration were to be given, it would be clear that there is no reason to include the legal profession with the other designated professions in the proposed legislation.
11. The Government acknowledged that as far as the solicitors are concerned, there is a high level of compliance in relation to AML issues. The Government informed the Law Society at the Consultation Session on 9 March 2017 that Hong Kong’s AML and terrorist financing criminal statistics, on the whole, are low. The Joint Financial Intelligence Unit also acknowledged that the suspicious transaction reports submitted by the solicitors are of high quality. Subjecting solicitors and foreign lawyers to the regulatory regime of the Anti-Money Laundering and Counter Terrorist Financing (Financial Institutions)

Ordinance (“AMLO”) will be out of proportion to the risk engendered by solicitors and foreign lawyers in Hong Kong in relation to money laundering and terrorist financing. The Government should adopt a “risk based approach” to the regulation of solicitors and foreign lawyers in relation to AML issues – they do not present a serious AML risk to Hong Kong so there is no pressing need to impose statutory requirements.

12. In the DNFBP Consultation Paper, the Government explained that it intended to leverage on the existing regulatory regime applicable to the legal profession under the LPO to enforce the CDD and record keeping requirements. The Paper also proposed that the Law Society take on statutory responsibility for monitoring and ensuring compliance with the AML requirements. The Government admitted that the LPO already stipulates a set of appropriate disciplinary and sanction measures which provide a sufficient deterrent effect in terms of the proportionality and dissuasiveness of relevant sanctions. The Government has said that it has no intention of proposing further criminal sanctions for non-compliance, having regard to the inherent AML risks. In these circumstances, the Law Society’s existing regulatory regime (based on the LPO and Practice Direction P) should continue to be used to implement the AML requirements with respect to solicitors and foreign lawyers.
13. As will have been noted from our submissions above, the legal profession is the only profession which already has enforceable AML regulations. Consequently, the inclusion of the legal profession in the draft legislation with the other sectors of the DNFBP which do not have such enforceable regulations is otiose.
14. Turning now to AML education and training, the Law Society conducts risk management education courses on AML issues annually. All solicitors, trainee solicitors and foreign lawyers working in Hong Kong firms are required to attend risk management education courses. In addition, the Law Society co-organises with the Government an annual seminar on AML issues for our Members. The most recent seminar was well received with more than 200 participants. The Chairman of the AML Committee was one of the speakers. The Law Society’s official monthly journal regularly features commentary on AML (and risk management issues). In terms of promotion of AML initiatives, the Law Society is the clear leader among the professions in Hong Kong.
15. Other international financial centres such as London and New York do not impose statutory provisions on solicitors (or lawyers) for CDD and record keeping requirements.

16. With the introduction of the AMLO in 2012, financial institutions are burdened with stringent statutory AML requirements. There is a perceived general sentiment that many of the account opening procedures and requirements adopted by the banks may be unnecessarily excessive and complicated, inflexible and time consuming. The frustrating experience in the first step of doing business in Hong Kong may be driving businesses away from Hong Kong. There is a concern that the AMLO is having a negative effect of undermining Hong Kong's status as an international financial centre. Likewise, if the Government tightens its regulatory regime on the legal profession by codification of CDD and record keeping requirements and/or introduction of criminal sanctions for non-compliance, law firms may be reluctant to open new files and take up new clients. Such draconian measures are disproportionate to the AML risks encountered by the legal profession.
17. For the above reasons, solicitors and foreign lawyers should be treated separately from the other DNFBP and should be excluded from the proposed legislation.

(B) *UNATMO Consultation Paper*

The Law Society has no comment (for now) on the UNATMO Consultation Paper. Further developments will be reviewed, in due course.

11 April 2017
The Law Society of Hong Kong

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