

REGULATORY UPDATES (FINANCIAL SERVICES) October 2019 Issue



To maintain the financial stability and facilitate the economic growth of Hong Kong, regulators have been reviewing and establishing different legal framework regularly for financial institutions. In this month, the Hong Kong Monetary Authority (HKMA), Securities and Futures Commission (SFC) and Insurance Authority (IA) have the following updates:

"Hong Kong has a strong legal and institutional framework for combating money laundering and terrorist financing." FATF commented

On 4 September 2019, the Financial Action Task Force (FATF) and Asia/Pacific Group on Money Laundering (APG) published a mutual evaluation report on the anti-money laundering (AML) and combating the financing of terrorism (CFT) measures of Hong Kong. FATF and APG commented that Hong Kong had a strong legal and institutional framework for combating money laundering and terrorist financing. The technical compliance framework is particularly strong regarding confiscation, law enforcement, preventive measures for and the supervision of financial institutions, and international co-operation but less strong regarding transparency of legal arrangements, preventive measures for politically exposed persons, and supervision of designated non-financial businesses and professionals (DNFBPs). FATF and APG made a number of recommendations on the AML/CFT regime of Hong Kong in the report. The recommendations include the following:

- The authorities should take additional steps to disseminate and communicate its ML/TF risk assessment to better ensure that the private sector, particularly DNFBPs, are aware of their ML/TF risks;

CONTENTS

- ▶ "Hong Kong has a strong legal and institutional framework for combating money laundering and terrorist financing." FATF commented
- ▶ HSBC reprimanded and fined HK\$2.1 million for telephone recording non-compliance
- ▶ Bank fined US\$4 million and its senior management replaced for violation of sanctions regulations
- ▶ SFC proposed regulatory regime for trustees and custodians

- HK should conduct targeted outreach to smaller entities in all sectors and focus in particular on those sectors that demonstrated more systemic gaps in understanding of their targeted financial sanctions obligations, such as money service operator; and
- HK should continue its ongoing efforts to review and update its understanding of ML/TF risks and should take steps to more closely review the ML threats arising from foreign crimes such as corruption, and tax crime.

In short, HK has a strong and effective framework on AML and CFT. However, smaller entities such as money service operators should also watch out for enhancing their current AML/CFT practices.

Read more on the following website:

<http://www.fatf-gafi.org/media/fatf/documents/reports/mer4/MER-Hong-Kong-2019.pdf>

HSBC reprimanded and fined HK\$2.1 million for telephone recording non-compliance

On 10 September 2019, the Securities and Futures Commission (SFC) disclosed that they reprimanded and fined The Hongkong and Shanghai Banking Corporation Limited (HSBC) HK\$2.1 million for non-compliance with the telephone recording requirements under the Code of Conduct issued by the SFC. The disciplinary action was due to failure in setting up voice recording of some telephone lines of its private banking division between 8 April 2017 and 31 January 2018. This involved 5,830 customer order instructions received via 59 telephone lines not being tape recorded.

The SFC considered that HSBC failed to put in place effective internal control procedures to ensure proper implementation of the telephone recording function and timely detection of any telephone recording failures.

Read more on the following websites:

<https://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=19PR82>

<https://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/openAppendix?refNo=19PR82&appendix=0>

Bank fined US\$4 million and its senior management replaced for violation of sanctions regulations

On 3 September 2019, the US Treasury Department's Office of Foreign Assets Control (OFAC) entered into a settlement agreement with British Arab Commercial Bank plc (BACB), a commercial bank located in London under which the bank agreed to pay a US\$4 million penalty to settle the potential violations and its obligations to pay OFAC.

Facts

- BACB which has no offices, business or presence in US, processed payments with apparent violations of the Sudanese Sanctions Regulations (SSR) totaling US\$191 million.
- OFAC determined that BACB did not make a voluntary self-disclosure of the apparent violations, and that these apparent violations constitute an egregious case.
- The total base penalty amount for the apparent violations was \$381,400,000.
- In consultation with BACB's domestic regulator in UK, OFAC determined that the Bank's operating capacity was such that it would face disproportionate impact if required to pay the proposed penalty.
- In view of BACB's operating capacity, the fact that it has represented that it ceased the conduct, its entering into a settlement agreement, and its maintenance of the compliance commitments articulated in the settlement agreement, BACB would remit US\$4 million to settle these potential violations and its obligations to pay OFAC.

The case

- Between September 21, 2010 and August 27, 2014, BACB processed 72 bulk funding payments totaling \$190,700,000 related to Sudan.
- BACB operated USD accounts on behalf of at least seven Sudanese financial institutions, including the Central Bank of Sudan. BACB actively solicited USD business from Sudanese banks, and processed these USD transactions via an internal book transfer process involving a nostro-account maintained at a foreign bank (Bank A) in Europe.
- *These transactions were not processed directly through the US financial system.* The process to fund its USD nostro account at Bank B did involve transactions processed to or through US financial institutions in apparent violation of US economic sanctions administered by OFAC which prohibited US banks, from processing such transactions.

Remedial measures

BACB took several remedial measures in response to the apparent violations, including:

- Withdrawal from the Sudanese market in late 2014;
- Replacing previous senior management with new hires (including Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, Chief Risk Officer, Chief Controls Officer, Chief Compliance Officer, and in-house General Counsel); and

- Updating the compliance program, processes and procedures regarding know your customer, anti-money laundering and sanctions.

These and other mitigating factors led to the final penalty amount of US\$4 million, which was reduced significantly from its original proposed penalty.

Read more on the following websites:

https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20190917_bacb.pdf

https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20190917_bacb_settlement.pdf

SFC proposed regulatory regime for trustees and custodians

On 27 September 2019, SFC issued a consultation paper on proposed regulatory regime for depositaries of SFC-authorized collective investment schemes (CIS).

Depositaries (ie trustees and custodians) of publicly offered CIS (or commonly known as 'funds') are usually restricted to banks or trust companies in Hong Kong. They are regulated by the corresponding regulations, but the provision of trustee or custodial services for CIS is not a regulated activity in Hong Kong.

The protection of fund assets has been a major concern since the global financial crisis. Regulatory authorities in many overseas jurisdictions have reviewed or reformed their safe custody regimes. Recommendations to clarify, modernise and further develop standards for the custody of assets managed under CIS was raised by the International Organization of Securities Commissions (IOSCO).

Trustees and custodians of public funds in Hong Kong are currently not subject to any specific licensing regime for. There is no direct on-going regulatory supervision of their trustee or custodial function for public funds. The lack of a specific, direct regulator gives rise to practical difficulties in ensuring appropriate regulation and supervision of these activities.

Accordingly, to better align with international practice and enhance the protection of investors in public funds, the SFC proposed to create a new regulated activity to bring trustees and custodians of public funds under the SFO licensing, supervision and enforcement regime applicable to intermediaries.

Read more on the following website:

<https://www.sfc.hk/edistributionWeb/gateway/EN/consultation/openFile?refNo=19CP3>

BDO'S SUPPORT AND ASSISTANCE

25th Floor, Wing On Centre
111 Connaught Road Central
Hong Kong
Tel: +852 2218 8288
Fax: +852 2815 2239
info@bdo.com.hk

RICKY CHENG
Director and Head of Risk Advisory
Tel: +852 2218 8266
rickycheng@bdo.com.hk

BDO Limited, a Hong Kong limited company, is a member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms.

BDO is the brand name for the BDO network and for each of the BDO Member Firms.

This publication has been carefully prepared, but it has been written in general terms and should be seen as broad guidance only. The publication cannot be relied upon to cover specific situations and you should not act, or refrain from acting, upon the information contained therein without obtaining specific professional advice. Please contact BDO to discuss these matters in the context of your particular circumstances. BDO, its directors, employees and agents do not accept or assume any liability or duty of care for any loss arising from any action taken or not taken by anyone in reliance on the information in this publication or for any decision based on it.