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Risk Assessment and Mitigation of Money Laundering , Terrorist Financing & Proliferation Financing

27 September 2022

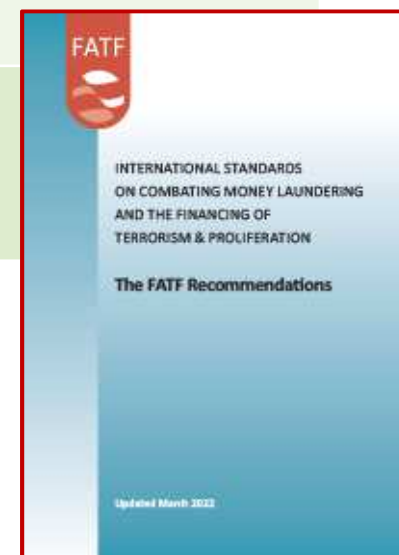
Money Service Supervision Bureau

Trade Controls Branch

Background

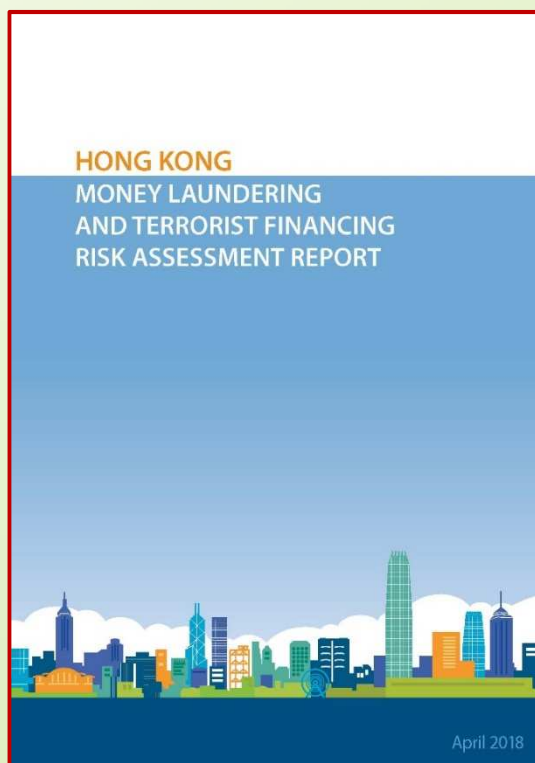
HONG KONG

- Member of the Financial Action Task Force (FATF) and Asia/Pacific Group on Money Laundering (APG)
- Response to the fast-changing financial-market and Anti-Money laundering landscapes
- Response to the FATF Recommendations on National Risk Assessment

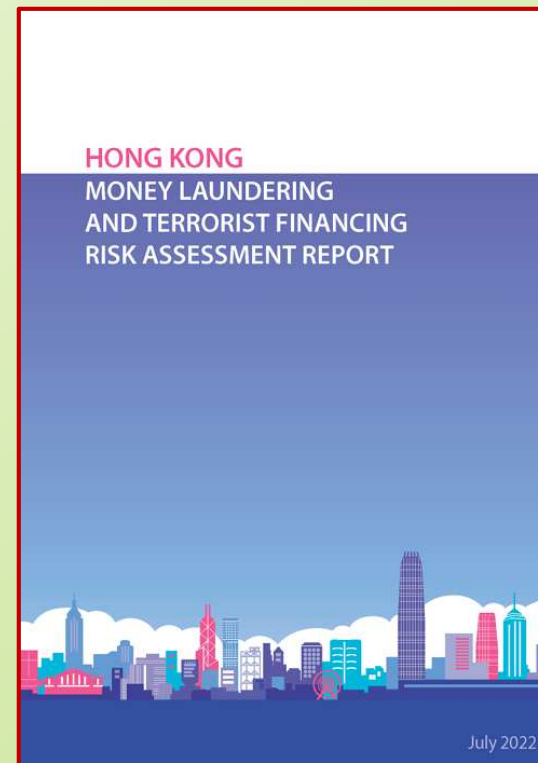


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Hong Kong Money Laundering and Terrorist Financing Risk Assessment Report (HRA)



2018 1st HRA

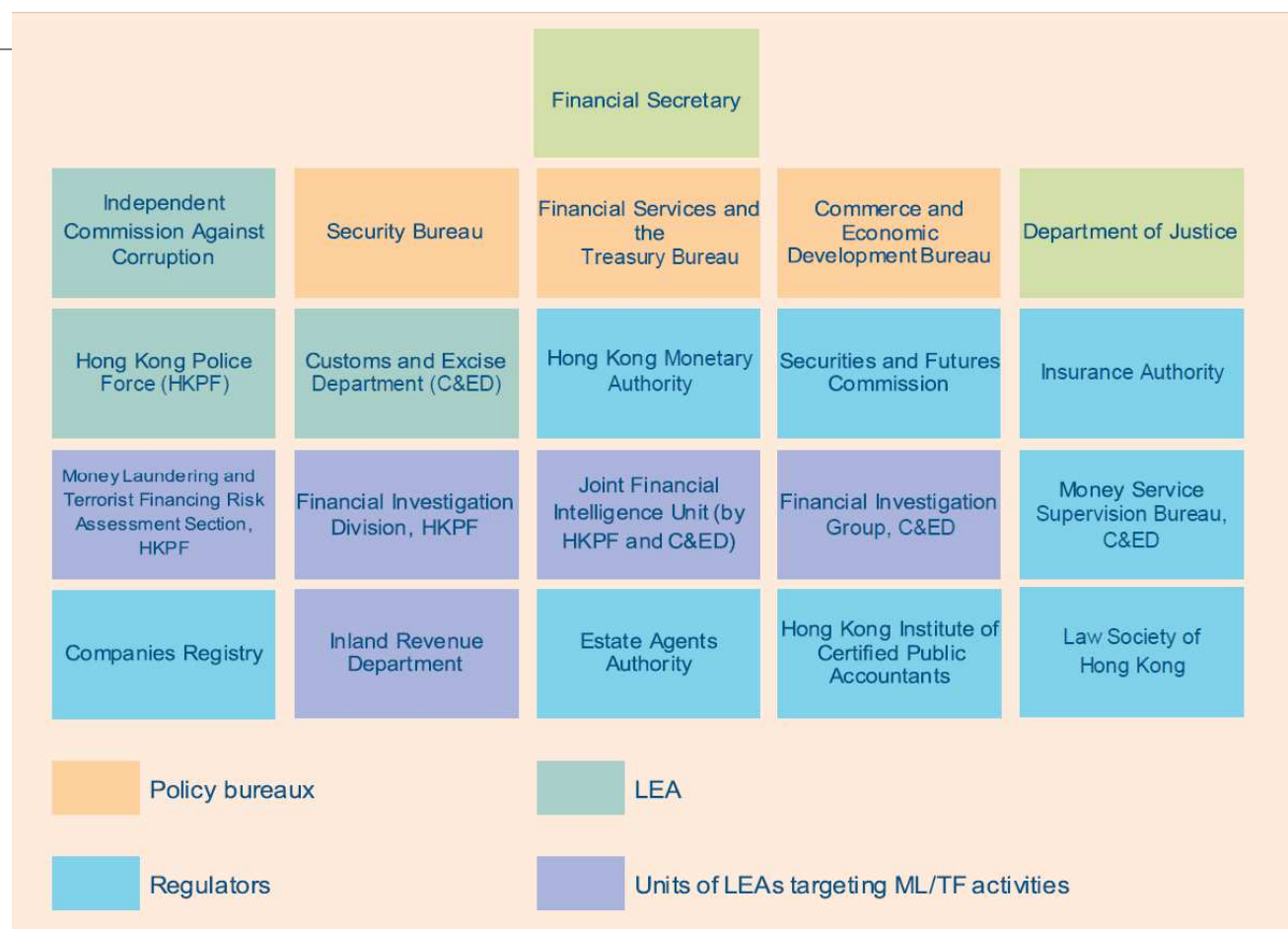


2022 2nd HRA



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Key Stakeholders in the Coordination and Implementation of AML/CFT Policies and Strategies



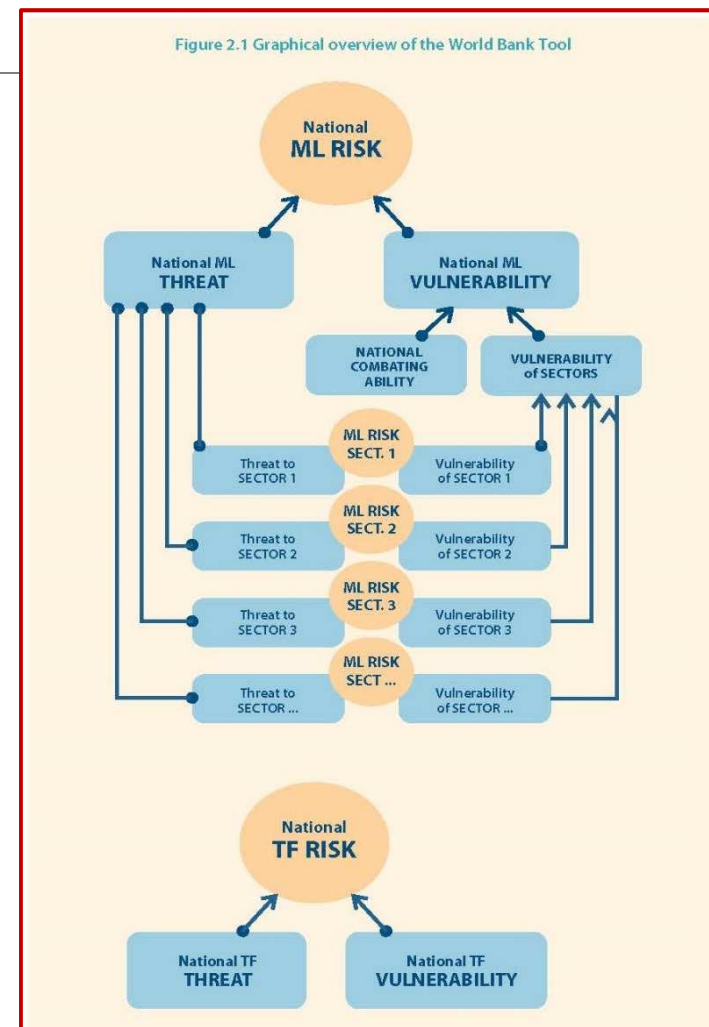
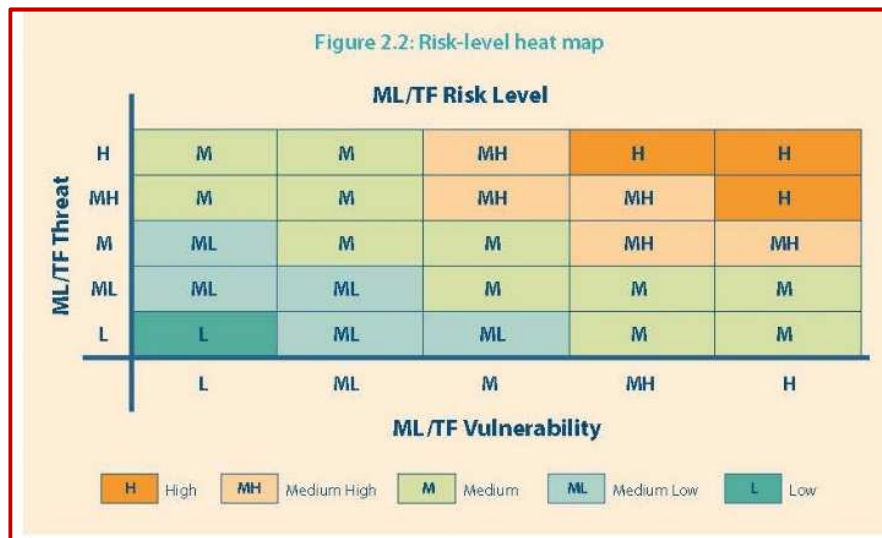
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Risk Assessment Methodology

FATF Guidance on National Money Laundering and Terrorist Financing Risk Assessment

World Bank National Risk Assessment Tool



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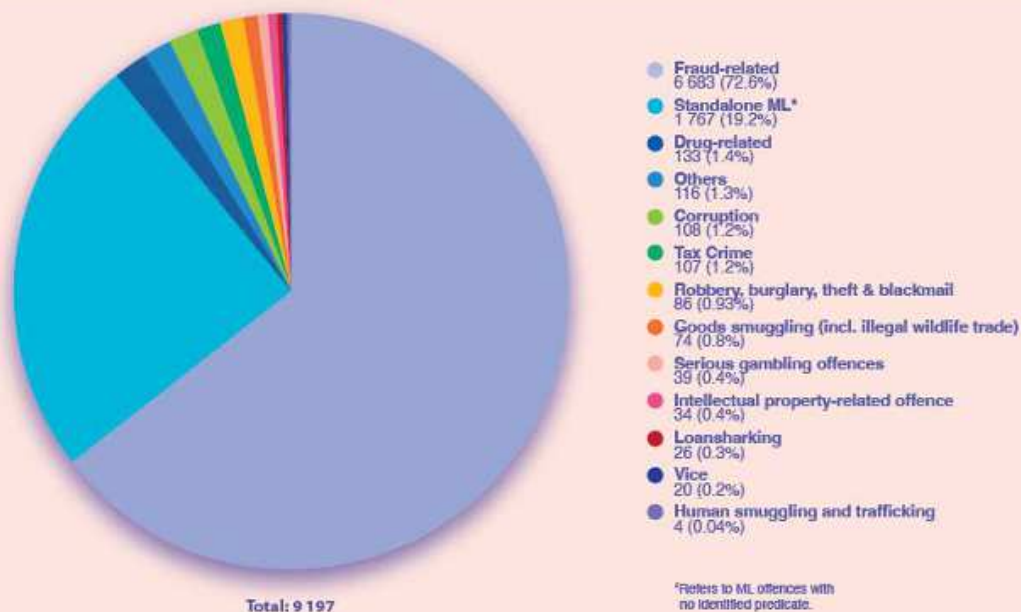
Key Findings – Money Laundering (ML)

Hong Kong's ML Threat

Medium-high

What are the
predicate offences
of ML cases?

Figure 4.1: Breakdown of ML Investigations initiated in 2016-2020
by predicate offences



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Key Findings – Money Laundering (ML)

Hong Kong's Ability to Combat ML

High



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Key Findings – Money Laundering (ML)

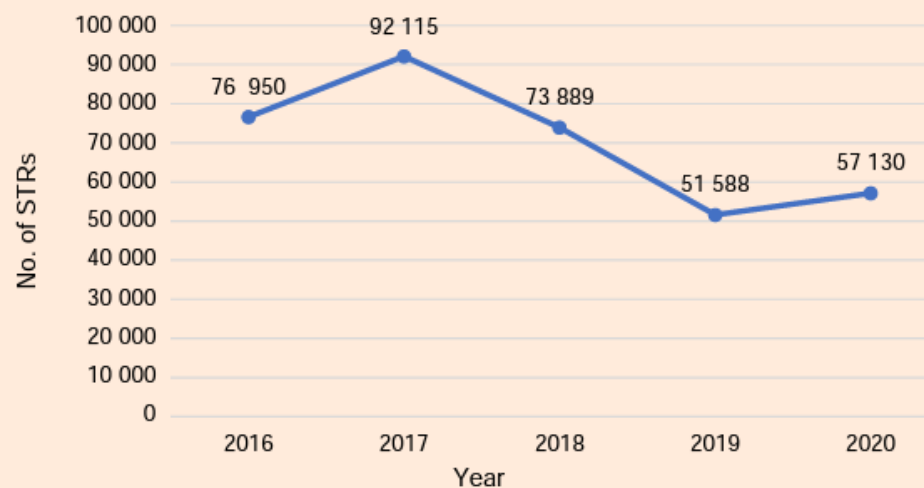
Hong Kong's ML Vulnerabilities

Improvement in the understanding of ML/TF risks and awareness of AML/CFT obligations

Improvement in the quality of the reports received

Figure 3.3: Number of STRs received by JFIU

Number of STRs Received from 2016 - 2020



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Key Findings – Money Laundering (ML)

Overall ML Risk of Hong Kong

A medium-high level of ML risk

A medium-high level of ML threat

A medium level of ML vulnerability



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Key Findings – Terrorist Financing (TF)

Overall TF Risk of Hong Kong

A medium-low level of TF risk

A medium-low level of TF threat

A medium-low level of TF vulnerability



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Way Forward

Five Major Areas of Work



Enhancing the
AML/CFT legal
framework



Strengthening risk-
based supervision
and partnerships



Stepping up outreach
and awareness-
raising



Monitoring new and
emerging risks



Strengthening law
enforcement efforts
and intelligence
capability

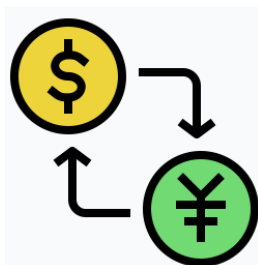


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Risk Assessment of MSO sector

- ◆ Definition of Money Service under the Anti-Money Laundering and Counter-Terrorist Financing Ordinance, Cap. 615 (“AMLO”)
- ◆ Landscape of Licensed MSOs



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ML Threats & Vulnerabilities of MSO sector

ML Threats

- ◆ Used in the placement and layering stages of ML
- ◆ Fraud (e.g. telephone deception, email scam and lottery fraud)
- ◆ Cybercrime

ML Vulnerabilities

- ◆ Cash-intensive nature with global exposure
- ◆ Frequent and cross-border transactions
- ◆ Large-amount transactions by walk-in and one-off customers
- ◆ Use of online platforms
- ◆ Transactions below customer identification and verification thresholds

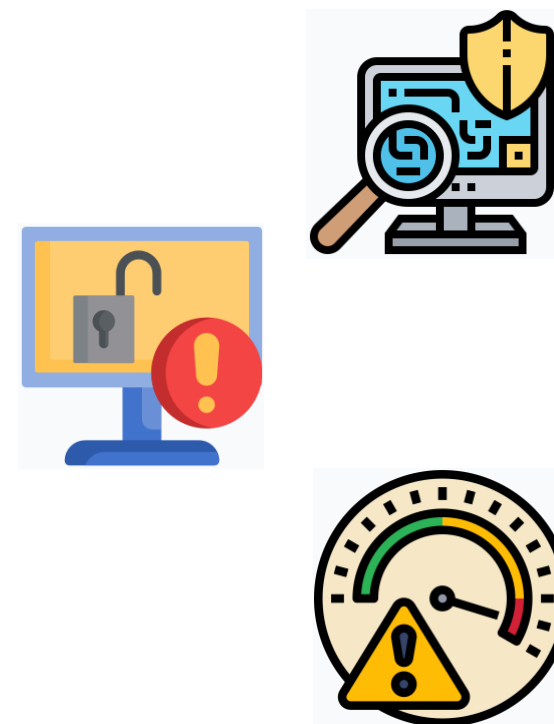


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Overall Risk of MSO Sector

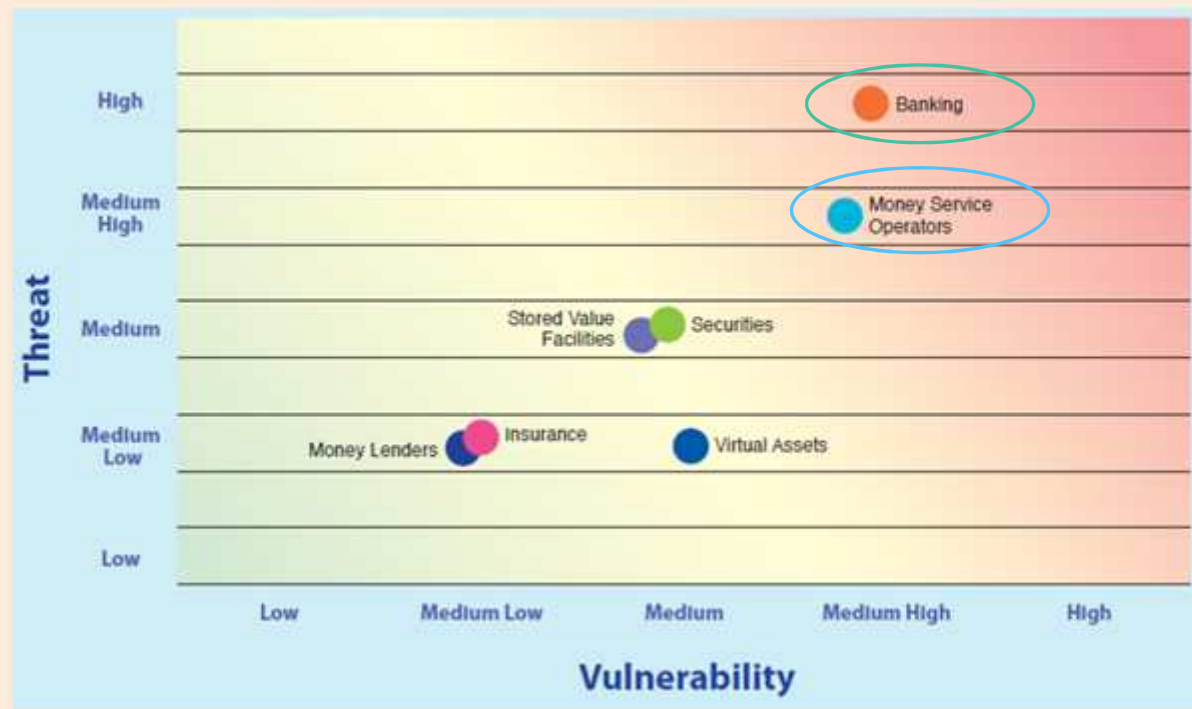
- ◆ ML threat : **Medium-high**
- ◆ Vulnerabilities : **Medium-high**
- ◆ Overall risk : **Medium-high**



Key Findings – Money Laundering (ML)

Hong Kong's ML Threat - Financial Sectors

Figure 5.2: Overview of risk levels of major financial institutions



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Supervision and Enforcement



Risk-based Approach

- Revamped risk profiling methodology
- Appropriate supervisory extent and priority



Entry control

- Background due diligence
- Fit and Proper



Ongoing risk-based supervision

- On-site and offsite inspections
- Disciplinary sanctions



Sanction screening and transaction monitoring system

- Database and screening tool



Unlicensed money service operation

- MSO licensee register
- Monitors higher-risk areas
- Increasing the sentencing level to a fine of HK\$1,000,000 and imprisonment for two years



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Proliferation Financing (PF)

Definition provided by Financial Action Task Force (FATF)

... providing funds or financial services which are used, in whole or in part, for the manufacture, acquisition, possession, development, export, trans-shipment, brokering, transport, transfer, stockpiling or use of nuclear, chemical or biological weapons and their means of delivery and related materials (including both technologies and dual use goods used for non-legitimate purposes)...



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Proliferation Financing (PF)

FATF Recommendation 7

- ◆ Implement targeted financial sanctions (TFS) to comply with United Nations Security Council resolutions
- ◆ In relation to the prevention, suppression and disruption of proliferation of weapons of mass destruction and its financing
- ◆ Rule-based for all transactions

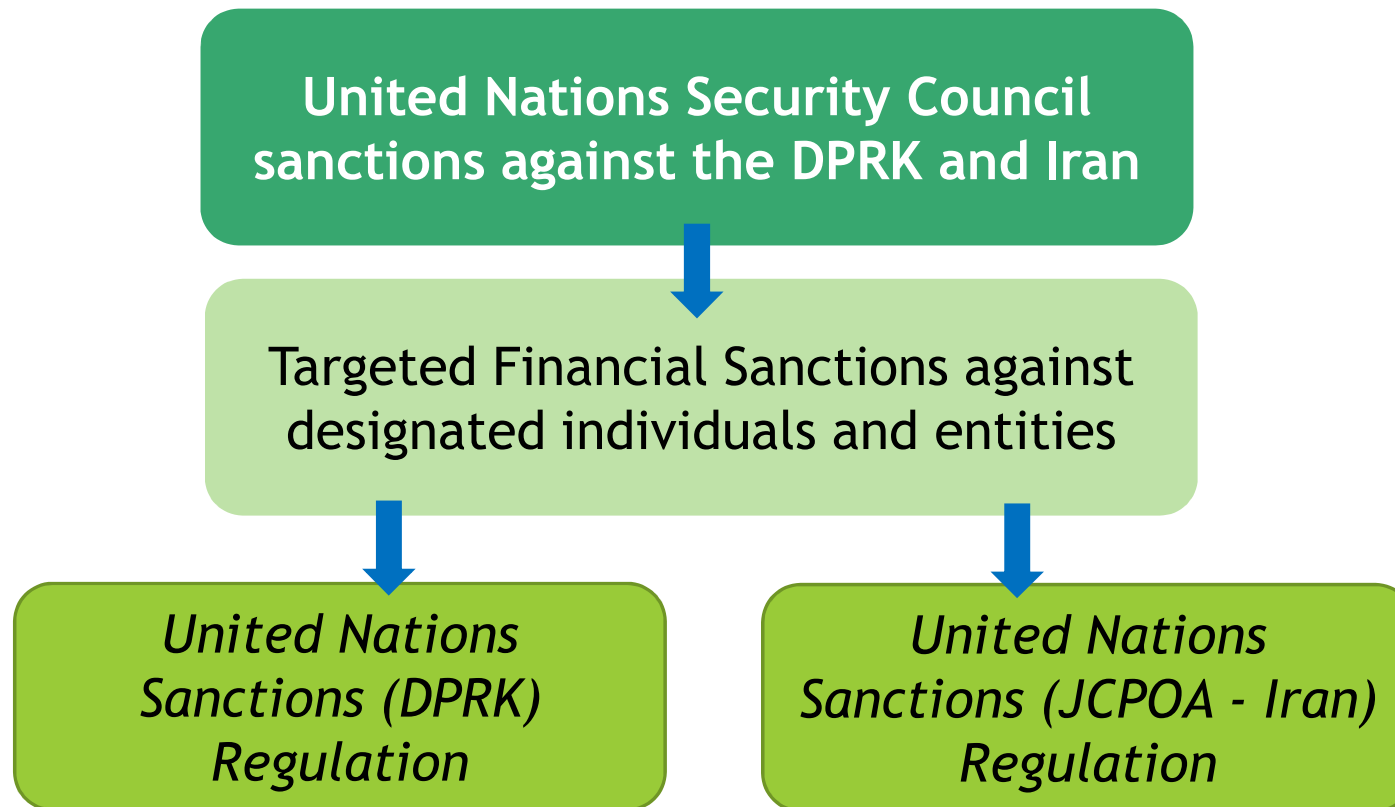


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Combatting PF

Targeted Financial Sanctions



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Combatting PF

Targeted Financial Sanctions

| Regime | Designated Persons | Designated Entities | Last Update by UN |
|-----------------------|--------------------|---------------------|-------------------|
| DPRK (North Korea) | 80 | 75 | Sep 2022 |
| Iran | 23 | 61 | Jan 2016 |



Website of the Commerce and Economic
Development Bureau for the sanction lists:
<https://www.cedb.gov.hk/tc/policies/united-nations-security-council-sanctions.html>



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Counter PF Regime in Hong Kong

Relevant legislations:

- ◆ Regulations made under the UNSO to DPRK and Iran
- ◆ Weapons of Mass Destruction (Control of Provision of Services) Ordinance (“WMDO”) (Cap. 526)
 - S.4 of WMDO prohibits a person from providing any services connected to PF
 - The provision of services includes the lending of money or other provision of financial assistance.



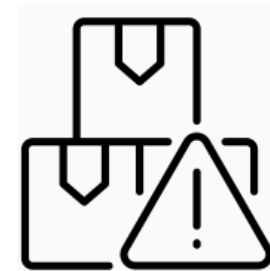
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Targeted Financial Sanctions

MSOs should not establish business relationship or conduct transactions with sanctioned individuals or entities.

MSOs should implement an effective screening mechanism, which should include screening customers and their beneficial owners against the most up-to-date sanction lists.



STR reporting to JFIU



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Proliferation Financing (PF)

Recent amendments to Recommendation 1 (RBA) by FATF -

- ◆ Jurisdictions and private sector entities are required to carry out **risk assessment and mitigation for PF of weapons of mass destruction**, in addition to the same requirements already imposed on ML & TF.



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PF Risk Assessment – Source of Information

◆ Some potential source of information:

- (1) FATF Mutual Evaluation Reports;
- (2) HRA Report;
- (3) UN Panel of Experts Report;
- (4) Sectoral Reports published by regulators



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PF Risk Assessment – Source of Information

◆ Some potential source of information (Cont'd):

(5) Government's databases;

(6) Commercial / Firm and Group-wide databases;

(8) Transaction record of dual-use / controlled goods

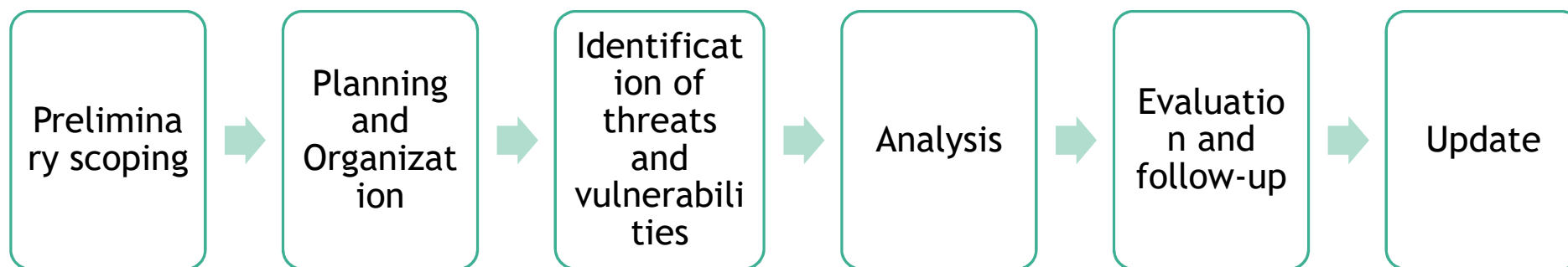


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PF Risk Assessment

- ◆ Similar to the process of an ML/TF risk assessment, but more targeted (narrower scope).
- ◆ The 6 key stages are:



(Source: 2013 FATF NRA Guidance and 2019 FATF TFRA Guidance)



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PF Risk Indicators

◆ Common high risk indicators:

Incomplete CDD
information

Reluctant to
provide
additional
information

Adverse news
related to
customers

Linkage with
universities /
research
institutions

Trading of dual-
use / controlled
goods / high-
tech products

Abnormal
transactions in
accounts

Jurisdictions of
customers



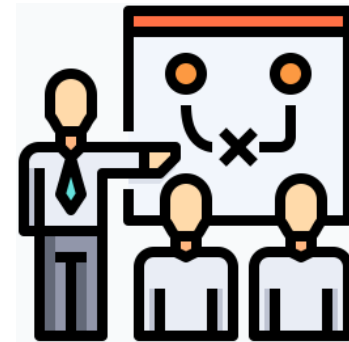
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Potential Risk of Evasion

◆ Tactics of evasion by designated persons / entities:

- (1) use of shell or front companies;
- (2) use of dummy accounts;
- (3) fraudulent intermediaries;
- (4) fraudulent businesses



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Action to mitigate PF

◆ An effective screening mechanism is crucial:

- screening its customers and any beneficial owners of the customers against the current sanctions lists; and
- screening its customers and any beneficial owners of the customers against all new and updated designations on the sanction lists.



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Key Findings – Proliferation Financing (PF)

Overall PF Risk of Hong Kong

A medium-low level of PF threat

A medium-low level of PF vulnerability

A medium-low level of PF risk



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Recommendations for MSO sector

- MSOs should:
 - Deepen understanding on PF risk and Targeted Financial Sanctions;
 - Be familiar with EDD (oversight by senior management)
 - File STR to JFIU



Way Forward

To enhance the supervision of the MSO sector by :

- a) strengthen its understanding of MSOs' risk profiles in order to form a solid foundation for effective risk-based supervision
- b) enhance MSOs' capability in particular in ML/TF/PF risk understanding, STR reporting obligations, and TF/PF TFS screening



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Way Forward

To enhance the supervision of the MSO sector by :

- c) encourage the adoption of innovation and new technology
- d) further study the emerging ML/TF/PF threats arising from cybercrime
- e) proactively conduct special theme-based review exercises



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Legislative Proposals

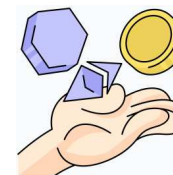
Two-tier Registration Regime for DPMS

- **Category A** registration is required for DPMS who do not intend to and will not engage in any cash transactions at or above HK\$120,000
- **Category B** registration is applicable to DPMS who intend to or may engage in any cash transaction at or above HK\$120,000



Licensing Regime for VASPs

- Designate the business of operating a VA exchange as a “regulated VA activity”
- Require any person seeking to engage in the regulated activity to obtain a VASP licence from the SFC



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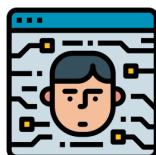
Legislative Proposals (cont'd)

Politically exposed persons (PEPs)

- To extend to PEPs in other parts outside Hong Kong (including the Mainland)
- To enable the adoption of a risk-based approach to determine whether to continue to apply the additional measures for foreign PEPs who are no longer entrusted with a prominent public function



Digital identification systems



- Assist the conduct of CDD in situations where a customer is not physically present for identification and verification purposes (i.e. non-face-to-face situations)

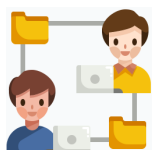
Penalty for unlicensed money service operation

- Raising the sentencing level to a fine of HK\$1,000,000 and imprisonment for two years



Exchange of supervisory information

- To standardize the parameters for exchange of information in the context of AML/CFT supervision among all AMLO regulators



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- The End -

Thank you !

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