

HKMA – Anti-Money Laundering Seminar

Customer Due Diligence Process for Offshore Companies

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HKMA - Industry Working Group (IWG)

- Represented by 20 banks and chaired by HKMA
- This should be the first paper on addressing the issue of customer due diligence process on offshore companies
- This was issued by HKMA on 31 Mar 2008
- Do not form part of the formal regulatory requirements but are practices expected to be adopted unless with equally effective alternative control measures

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Introduction

- **Authorized Institutions (AI) are required under HKMA's guideline to have effective customer due diligence (CDD) procedures to identify beneficial owners of their customer and verify their industry.**
- **Paragraph 5.11 of the Guideline on Prevention of Money Laundering provides that :**

“The following documents or information should be obtained in respect of corporate applicants for business which are registered in Hong Kong (comparable documents, preferably certified by qualified persons such as lawyers or accountants in the country of registration, should be obtained for those applicants which are not registered in Hong Kong) –

- (a) Certificate of Incorporation and Business Registration Certificate;*
- (b) Memorandum and Articles of Association;*
- (c) Resolution of the board of directors to open an account and confer authority on those who will operate it; and*
- (d) A search of the file at Company Registry.” (emphasis added)*

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Introduction (cont'd)

Paragraph 4.5 of the Supplement to the Guideline (the Supplement) further states that:-

“In relation to a company which is not listed on a recognised stock exchange (or is not a subsidiary of such a listed company) or not a state-owned enterprise or is a non-bank financial institution other than those mentioned above in paragraph 4.4, an AI should look behind the company to identify the beneficial owners and those who have control over the funds. This means that, in addition to obtaining the documents specified in paragraph 5.11 of the Guideline, the AI should verify the identity of all the principal shareholders, at least two directors (including the managing director) of the company and all its account signatories.” (emphasis added)

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Introduction (cont'd)

Knowing that company laws and regulations vary from jurisdiction to jurisdiction, the HKMA has given some degree of flexibility to AIs in opening accounts for offshore companies. Specifically, Interpretative Notes No.16 (IN 16) provides that:-

“AIs may rely on the documentation provided by professional third parties (such as lawyers, notaries, actuaries, accountants and corporate secretarial service providers) in Hong Kong on behalf of a corporate customer incorporated in a country where company searches are not available, provided that there is no suspicion arising from other information collected and these professional third parties can meet the criteria set out in paragraphs 6.3 and 6.4 of the Supplement and IN 28 below.” (emphasis added)

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Why diligence process on offshore companies is an issue?

- Different jurisdictions may have different company formation requirements and documentation.
- Unlike company registered in HK, Company search reports are difficult to obtain or unavailable.
- Certificate of Incumbency (COI), or equivalent, can be used to identify the directors and principal shareholders of a company. However, there is implication on cost and a COI can only provide information on one layer of the company's information (e.g. is that necessary to obtain COI for each layers?).
- IN 16 permits Als to rely on the documentation provided by professional third parties in Hong Kong, however, such professional third parties are not able to assist if they were not involved in the formation of the company or they are currently serving the company.
- In view of different practices, banks also facing a problem that customer would complain "such is not required when I open my account in another Bank!".

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Level Playing Field

More guidance is needed on due diligence process for offshore companies. Key recommendations in the IWG paper on CDD for offshore companies are:

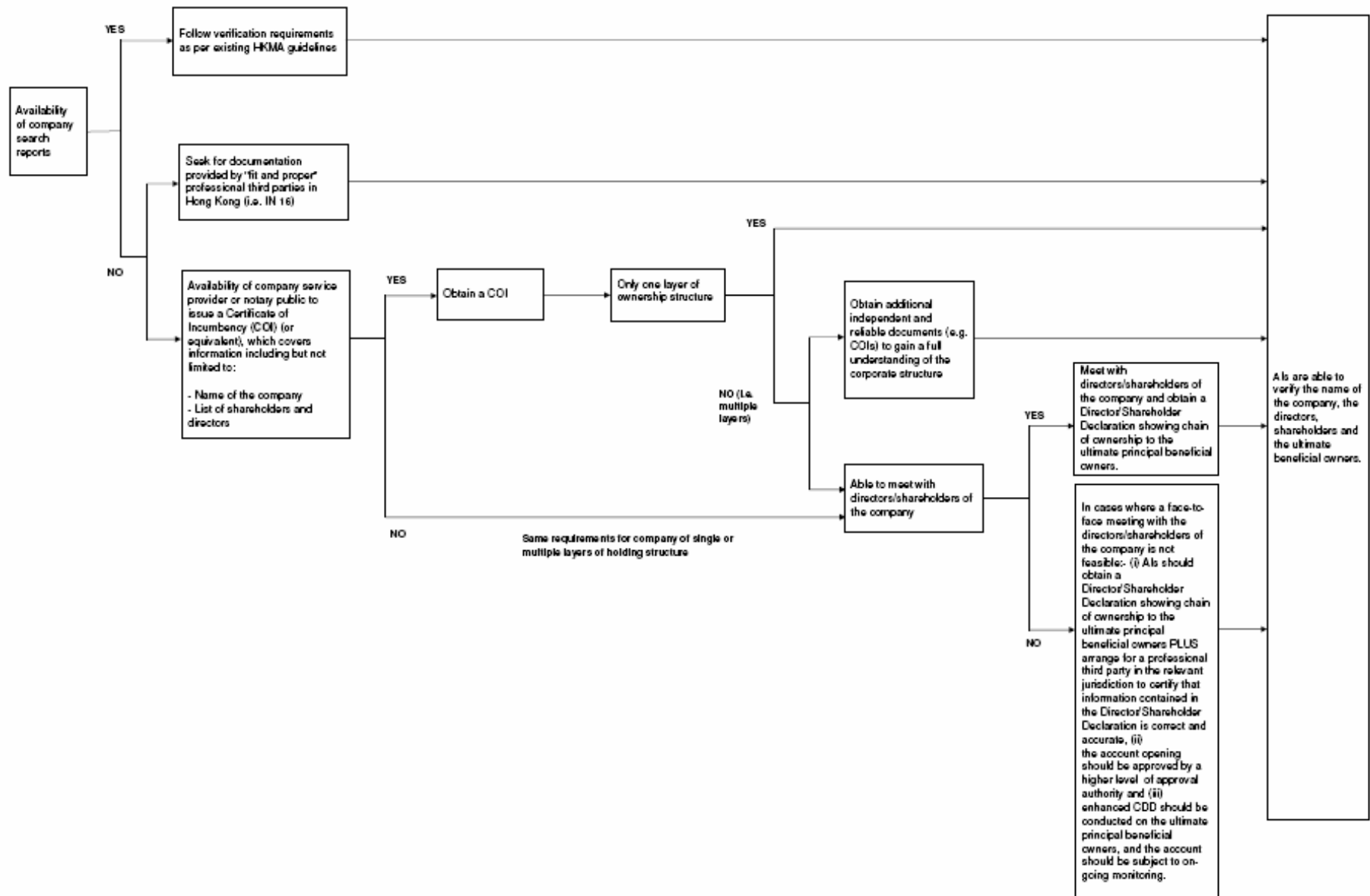
- Certificate of Incumbency (COI), or equivalent, should be obtained when available (e.g. BVI and Cayman). This would create a level playing field for all Als as it will become a standard expense for each customer.
- The Paper also recommend alternative processes for offshore company with multiple layers or when COI is not available

The recommended due diligence process is best described by a process flowchart.

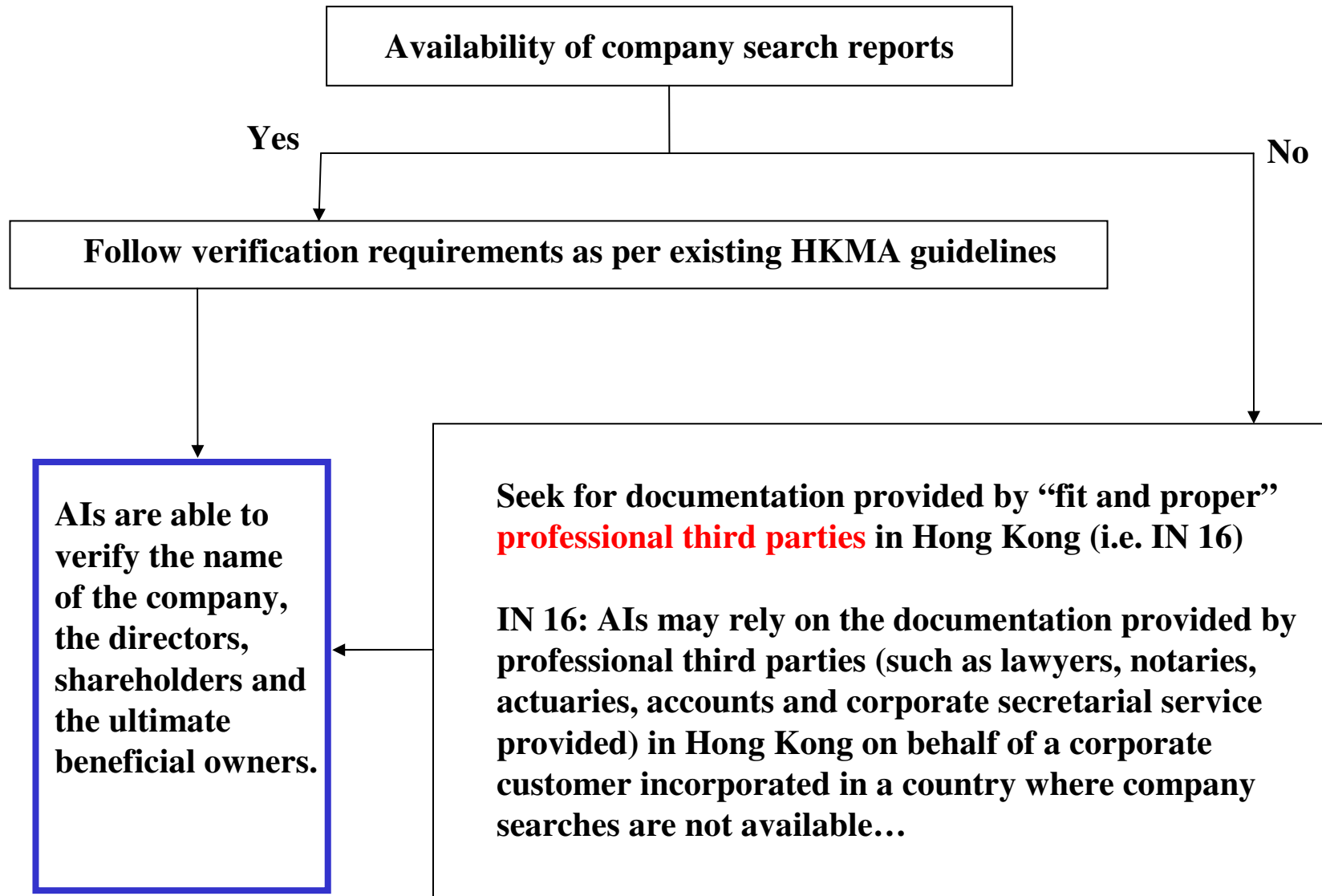
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Annex

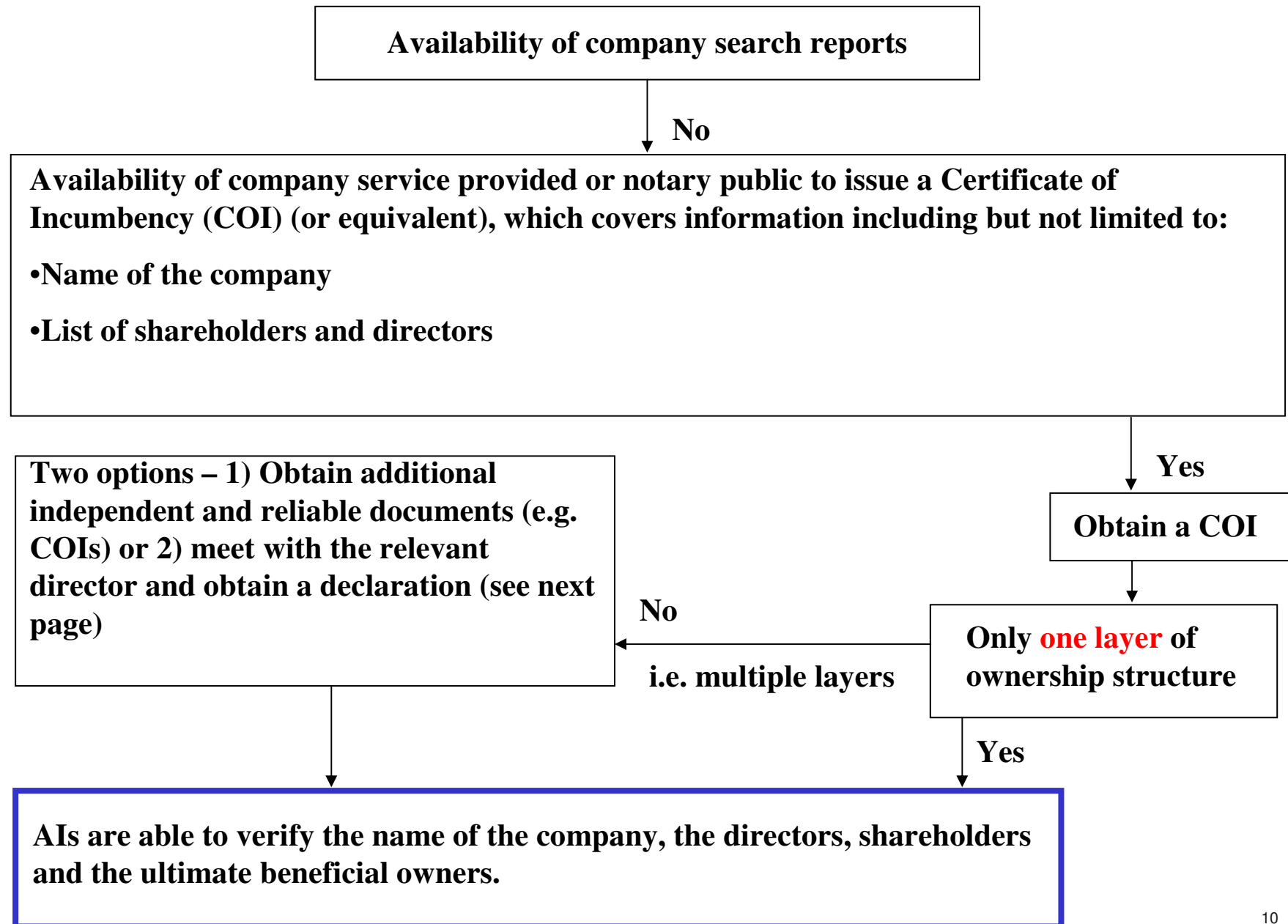
Flowchart on Account Opening for Offshore Companies



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Availability of company service provided or notary public to issue a Certificate of Incumbency (COI) (or equivalent), which covers information including but not limited to:

- Name of the company
- List of shareholders and directors

No

Multiple Layer or COI not available

Able to meet with directors / shareholders of the company

Yes

Meet with directors / shareholders of the company and obtain a **Directors / Shareholder Declaration** showing chain of ownership to the ultimate principal beneficial owners.

AIs are able to verify the name of the company, the directors, shareholders and the ultimate beneficial owners.

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No COI and not able to meet
with directors / shareholders
of the company

In case where a face-to-face meeting with the directors / shareholders of the company is not feasible:- (i) AIs should obtain a **Director / Shareholder Declaration** showing chain of ownership to the ultimate principal beneficial owners **PLUS** arrange for a professional third party in the relevant jurisdiction **to certify** that information contained in the Director / Shareholder Declaration is correct and accurate, (ii) the account opening should be **approved by a higher level** of approval authority and (iii) **enhanced CDD** should be conducted on the ultimate principal beneficial owners, and the account should be subject to on-going monitoring.

AIs are able to verify the name of the company, the directors,
shareholders and the ultimate beneficial owners.

Conclusion

The IWG believes that the adoption of the above industry standards would strike an appropriate balance between the need to identify and verify the identity of beneficial owners on the one hand and enabling AIs to provide efficient banking services to offshore companies from different jurisdictions on the other. This is important to maintaining the status of Hong Kong as an international financial centre.