

31 May 2018

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To: Chief Executive of all authorized insurers
carrying on long term business

Dear Sirs,

Key Findings of AML/CFT Onsite Inspection Visits to Authorized Insurers Carrying on Long Term Business

The Insurance Authority (“IA”) is responsible for overseeing the compliance of, amongst others, authorized insurers carrying on long term business (“insurers”) with the relevant requirements under the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Cap. 615) (“AMLO”) and the Guideline on Anti-Money Laundering and Counter-Terrorist Financing (“the Guideline”) issued thereunder.

The IA considers onsite inspection visit is an important supervisory tool to gauge the level of compliance by insurers. As such, various onsite inspection visits have been conducted to more than twenty insurers to review their Anti-Money Laundering and Counter-Financing of Terrorism (“AML/CFT”) policies, procedures and controls (collectively referred to as “AML/CFT systems”) and their compliance with the AMLO and the Guideline.

Although it was noted that insurers, in general, had appropriate AML/CFT systems in place, requisite improvements in certain areas would be necessary. With a view to raising the standards of the insurance industry in this respect, the IA would like to share with you some key findings as identified in the aforementioned onsite inspection visits. The details of which are summarized at the Annex for your attention. Key areas for improvement include:-

- 1) Senior management oversight;
- 2) Compliance functions;
- 3) Customer risk assessment;
- 4) Customer due diligence process;
- 5) Screening of Politically Exposed Persons, terrorists and sanction designations;
- 6) Ongoing monitoring;
- 7) Suspicious transaction reporting; and
- 8) Staff/insurance agent training.

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The IA wishes to emphasize that the senior management of any insurer is responsible for oversight of the AML/CFT function. Section 2.11 of the Guideline stipulates that senior management should be satisfied that the AML/CFT systems are capable of addressing relevant money laundering and terrorist financing risks. Senior management oversight is an essential and integral part of AML/CFT system.

In respect of the issues identified, the insurers concerned have been requested to take remedial actions which are subject to further follow-up reviews by the IA.

The IA will continue its focus on AML/CFT compliance and will assess insurers' compliance on an ongoing basis through conducting inspection visits and use of other supervisory tools. Meanwhile, IA will also continue to provide guidance to facilitate the insurance sector in understanding and complying with the AML/CFT obligations through seminars/briefings and circulars, etc.

Should you have any enquiries regarding the above, please contact Mr Dickson Chui at 3899 9716 or Mr Raven Chan at 3899 9754.

Yours faithfully,

Stephen Po
Executive Director
Market Conduct Division
Insurance Authority

Encl.

c.c. Chairman, The Hong Kong Federation of Insurers

Summary of Key Inspection Findings

1) Senior management oversight

a) Compliance review and resources

In order to discharge their oversight function, senior management should, as far as practicable, ensure that the Compliance Officer (“CO”) and Money Laundering Reporting Officer (“MLRO”) are equipped with sufficient resources.

It was noted that some requisite compliance reviews were not timely conducted by compliance function (delayed by more than 9 months in one case). This had been attributed to staff turnover and tight manpower resources in compliance function.

Senior management should ensure adequate resources are deployed in compliance function at all times so that the AML/CFT responsibilities are fully and effectively carried out. Compliance reviews should also be regularly conducted as planned, with the completion timeline of such reviews specified and strictly followed to avoid any undue slippage and backlog.

b) Rectification of AML/CFT matters

Senior management is responsible for ensuring that the AML/CFT system is capable of addressing the money laundering and terrorist financing (“ML/TF”) risks identified. It was however noted in some cases that the rectification process for certain identified gaps or deficiencies was completed/yet to be completed with repeated postponement of target timelines (over a year in one case), or simply outstanding for a substantial period of time (over a year in another case). In some cases, subsequent recurrence of non-compliance were noted.

Senior management should diligently and vigilantly monitor the rectification progress of the AML/CFT compliance matters to ensure the remedial actions are taken timely, delivered on schedule and without undue slippage.

c) Policies and procedures

Various issues in the AML/CFT policies and procedures of some insurers were noted:-

- (1) Requisite Customer Due Diligence (“CDD”) requirements were not stipulated (e.g. no enhanced due diligence (“EDD”) measures were set out for domestic Politically Exposed Persons (“PEPs”) who were assessed to present a higher ML/TF risk; the advice of the insurer’s CO was not obtained in the senior management approval process of PEP cases; recording of the names of directors of corporate customers was not specified);

- (2) CDD requirements were incorrectly stipulated (e.g. PEP was incorrectly/unclearly defined; identification of customer was done after having established the business relationship); and
- (3) Repealed AML/CFT terms were used (e.g. using of the word “Fund” instead of “Property” in the definition of Terrorist Financing, and using the term “Non Cooperative Countries and Territories” instead of “Jurisdictions that do not or insufficiently apply the FATF Recommendations”).

Complete, accurate and updated AML/CFT policies and procedures form the basis of an effective AML/CFT system. Senior management should be diligent in approving such policies and procedures.

d) Enhanced due diligence measures for high risk customers

For customers classified as high risk, EDD measures including senior management approval should be taken before establishing the business relationship. It was however noted from some insurers’ practices that the requisite approvals were either not obtained or only obtained after establishment of the business relationship.

Senior management should pay special attention to any situation that by its nature presents a higher risk of ML/TF. They should ensure appropriate measures are in place so that their approvals have been timely obtained for the aforesaid situation.

2) **Compliance functions**

It was noted in some insurers that:-

- (1) Compliance reports on AML/CFT related matters were not regularly submitted to senior management or simply remained outstanding for a considerable period of time (over 1 year in one worst case);
- (2) Updates on certain AML/CFT matters, including material issues identified under compliance reviews (e.g. inadequate due diligence to identify potential ML/TF transactions) were not reported in the compliance reports to senior management; and
- (3) Inaccurate/Incomplete information on AML/CFT matters (e.g. information of high risk customer) was stated in the compliance reports to senior management.

Compliance functions should communicate key AML/CFT issues to senior management for its oversight. To ensure the process is effective, there should be proper controls on the regularity of the submission of compliance reports to senior management and the accuracy and completeness of relevant updates therein is adequate.

3) Customer risk assessment

Insurers should determine the extent of CDD measures and ongoing monitoring using a risk-based approach by considering all relevant risk factors, with such risk assessments duly documented. Whilst in general insurers have stipulated in their AML/CFT policies and procedures the requisite risk factors, it was however noted that:-

- (1) Such risk assessment was not actually conducted by some insurers;
- (2) Certain of the risk factors (e.g. product/service risk and delivery/distribution channel risk) were not considered in determining the overall ML/TF risk rating of customers; and
- (3) The risk factors were not/inaccurately rated (e.g. customer risk was not rated and marked as “not applicable”; AML risk score assigned did not properly reflect the underlying ML/TF risk).

Without conducting risk assessments and ensuring all relevant risk factors are considered and accurately rated, the extent of subsequent CDD measures and ongoing monitoring could not be properly determined to mitigate the relevant risks. It would be essential for senior management to diligently review the vigilance in the application of the risk assessment procedure by their staff.

4) CDD process

a) CDD information/documents obtained before business relationship is entered into

In respect of corporate customers, especially for those taking out group life insurance, some insurers failed to obtain the requisite CDD information/documents required under the Guideline (e.g. certificate of incorporation, the memorandum and articles of association, the company search report and the written authority to verify that account signatory was so authorized to represent the corporate customer).

For change of policyownership of individual life business, some insurers failed to obtain CDD information in respect of the proposed new policyholders (e.g. nationality/place of incorporation and information of the purpose and intended nature of the business relationship).

Insurers should tighten the control on CDD compliance to ensure that all requisite information/documents of policyholders are duly obtained.

b) Financial evidence of policyholders

Some insurers did not require financial status evidence (e.g. income/ assets proofs) of the policyholders for insurance policies reaching a high premium amount (e.g. in some cases, the premium amount threshold was set over HKD 6 million). In addition, the threshold specified by most insurers was on a per policy basis without consideration on a per person basis, i.e. requirement to be triggered in respect of all the insurance policies applied for and taken out by a policyholder.

Insurers should review the criteria setting with the view to tightening the specification threshold of obtaining income/assets proof and should implement it on a per person basis as a more effective way to ascertain total risks involved.

c) Copies of customer identification documents

The copies of identification documents (e.g. HKID card / passport images) of policyholders / beneficial owners / account signatories maintained in the record systems of some insurers were not in good quality (i.e. either blurred / darkened), which cast doubt on whether their identities have been well verified.

Insurers should ensure that they receive sufficiently clear copies of identification documents from customers or via insurance intermediaries and that the scanned images are of good quality which should then be properly recorded and maintained in their system.

5) Screening of PEPs, terrorists and sanction designations

It was noted in certain cases that there were absence or incompleteness in requisite screening on policyholders/ beneficial owners at the time of establishment of business relationship or on an ongoing basis. In most cases, ongoing batch screening on beneficial owners was not conducted due to the fact that the information of beneficial owners was not captured in the insurer's policy administration system, notwithstanding such information has been collected in the insurance application forms. In other cases, the reviews remained outstanding for a considerable period of time (i.e. generally over 1 month, and in one worst case, about 18 months).

Sanction violation is an offence whilst EDD is required for business relationship with PEPs. It is therefore essential for insurers to institute procedures to perform comprehensive initial and ongoing screening of its records to identify PEPs, terrorists and sanctioned parties for subsequent action. Adequate resources are also expected to deploy to conduct the requisite reviews timely to avoid violation of laws and the Guideline.

6) Ongoing monitoring

a) Monitoring of customer transactions and activities

Effective ongoing monitoring of customers' activities is an integral part of AML/CFT system. It helps insurers to know their customers and to detect unusual or suspicious activities. Several issues were noted that:-

- (1) Requisite ongoing monitoring measures (e.g. exception reports and transaction monitoring systems) were either not conducted or only conducted recently (e.g. more than 3 years since the commencement of the Guideline);
- (2) The pre-defined criteria used in certain monitoring systems had not captured any transactions across the period under review;
- (3) No exception reports were generated for suspicious transaction patterns (e.g. frequent changes of policyownership or those involving payout shortly after change of policyownership); and
- (4) The reviews conducted were not properly documented with necessary details, e.g. the name of the staff who conducted the review, date of review, matters reviewed, rationale of conclusion made, and next course of action to be taken.

Given the above issues noted, potential risks of ML/TF might not be properly mitigated on a timely manner. Insurers should ensure effective exception reporting mechanism is in place and the reports generated should be reviewed accordingly with proper documentation standards to detect any possible suspicious transactions.

b) Data capture on nationalities/ countries of residence/ places of incorporation

Whilst information of policyholders' nationalities/ countries of residence/ places of incorporation was obtained in the insurance application forms, it was noted that such information was not captured in some insurers' policy administration system. In other cases, the lists of the abovementioned information available to be selected in the policy administration system were noted not comprehensive enough and did not cover all jurisdictions that do not or insufficiently apply the FATF Recommendations¹, resulting in the abovementioned information recorded as "Others" in the policy administration system without further details.

As such, any business relationships with persons or entities from higher risk jurisdictions could not be ascertained through insurers' ongoing monitoring process. The insurers should hence ensure the abovementioned information of the policyholders is input in the policy administration system and that they are specific for effective ongoing monitoring purpose.

¹ From time to time, the IA issues circulars to update the insurance industry on jurisdictions that do not or insufficiently apply the FATF Recommendations according to the public statements issued by the Financial Action Task Force on Money Laundering.

c) Annual review

All high-risk customers including foreign PEPs and domestic PEPs assessed to present a higher risk should be subject to a minimum of an annual review of their profiles to ensure the CDD information retained remains up-to-date and relevant. It was however noted that such annual review was not conducted by some insurers. In other cases, there were no requisite procedures taken in the annual review to achieve the aforesaid purpose. In this connection, insurers should institute appropriate controls and procedures for complying with the aforementioned requirement.

d) Trigger events and reviews

An insurer should undertake review of existing records of policyholders upon trigger events to ensure that the information obtained is up-to-date and relevant, with the factors determining the period of review or what constitutes a trigger event clearly defined in the policies and procedures. However, it was noted in some instances that neither the requisite trigger events were set out nor the requisite reviews were conducted accordingly. Insurers should set out the requirements in their policies and carry out the reviews in actual practice.

7) **Suspicious transaction reporting**

a) Suspicious transactions reports (“STRs”) records

It was noted in some internal STRs of an insurer that the rationale for not reporting the case to the Joint Financial Intelligence Unit (“JFIU”) was not set out. In another instance, an insurer did not keep a full record of all disclosures (i.e. STRs) made to JFIU.

It is vital for MLROs to keep proper records of their deliberations and actions taken to demonstrate they have acted in reasonable manner. Meanwhile, insurers must also establish and maintain a record of all disclosures made to the JFIU.

b) Timing of reviewing STRs

An insurer was found to have considerable delay (i.e. over 1 month) in reviewing the internal STRs without apparent justification.

Insurers should ensure any STRs are reviewed timely and make a disclosure to the JFIU on any suspicious transaction as soon as practicable.

c) Acknowledgement of receipt and tipping off reminder

The MLRO of an insurer did not provide acknowledgement of receipt for STRs and the reminder of the statutory obligation not to tip off to the relevant reporting staff.

In this regard, insurers should ensure that they put in place internal controls to mitigate the potential risk of committing tipping off offence by their staff. On the other hand, insurers should communicate to or remind their staff and insurance agents of the tipping off offence and consequences through induction and refresher trainings.

8) Staff/insurance agent training

a) Training policy and attendance

It was noted that induction and refresher training policy and schedules were not set out by some insurers for their staff and insurance agents. It was also noted in other insurers that certain number of insurance agents had no records of attendance of any AML training. Amongst those that did attend the requisite training, it was found that the training was only completed after more than 6 months of joining the insurer.

Insurers should implement a clear and well articulated AML/CFT training policy, and should ensure that relevant staff and insurance agents attend the training timely to acquire and update their knowledge in this respect.

b) Training content and assessment

The AML/CFT training materials used by some insurers did not fully cover the personal statutory obligations and the possible consequences for failure to report suspicious transactions, as well as possible consequences of breaches of other statutory and regulatory obligations by staff and insurance agents, under various ML/TF legislations. It was further noted in some insurers that the assessment quizzes used to test the level of understanding of AML/CFT were over simplified and did not cover the abovementioned areas.

Insurers should review the training materials used to ensure they are comprehensive enough to cover all essential AML/CFT knowledge. The depth and coverage of assessment used should also be appropriate to ensure the effectiveness of the training is properly monitored.