

# Reporting suspicions about proceeds of crime

In Hong Kong the Drug Trafficking (Recovery of Proceeds) Ordinance (Cap.405) ('DTROP') and the Organised and Serious Crimes Ordinance (Cap.455) ('OSCO') require persons to report their suspicions about property being the proceeds of crime or intended to be used for the commission of crime.<sup>1</sup> This statutory duty applies to accountants who are used by money launderers.

## A. 'Gatekeepers'

1. Banks will always be used by money launderers because there is no better means to efficiently and economically launder proceeds of crime. However, as banks became increasingly diligent in their detection, monitoring and reporting of suspicions about transactions or property that may be connected to proceeds of crime, it is necessary for money launderers to resort to alternate means for laundering proceeds of crime. For this purpose, they look to 'Gatekeepers'.
2. The term 'Gatekeepers' describes persons and businesses who are used by money launderers to provide services and advice which assist them in the laundering of proceeds of crime. Principally, they include lawyers, accountants and tax advisors, as well as trust and corporate service companies.
3. Lawyers and accountants bring an appearance of respectability to a transaction or business operation - a useful disguise for money launderers. As well, law and accounting firms have offices or associations in many parts of the world which give money launderers a global reach.
4. Lawyers offer a range of services, such as client accounts, incorporation of companies (including offshore companies), and setting up of trusts which are useful to money launderers. Accountants and tax advisors are used by money launderers for the services they offer and for their expertise in

structuring transactions which can disguise the source of funds. Trust and corporate service companies are used by money launderers for the incorporation and maintenance of companies, and opening and operation of bank accounts. Their attractiveness to money launderers is that they are usually unregulated and not bound by regulatory regimes or codes of conduct.

## B. Financial Action Task Force

### 1. 40 Recommendations

5. The Financial Action Task Force ('FATF') is an international inter-governmental body whose mandate is to develop and promote policies to combat money laundering. Its policies aim to prevent proceeds of crime being utilised for future criminal activities or allowing criminals from retaining benefits derived from the commission of crime, and to prevent funds coming into the possession of terrorists.
6. In 2001 the FATF issued a report on money laundering typologies: 'Financial Action Task Force on Money Laundering – Report on Money Laundering Typologies 2000-2001'. It identified lawyers and accountants (amongst others) being used by money launderers and referred to them as 'Gatekeepers'. Paragraph 32 of the Report stated:

32. *The continuing effort by governments to combat money laundering has made*

*the work of the money launderer more difficult. In part as a means of circumventing money laundering counter-measures, launderers have had to develop more complex schemes. This increase in complexity, the FATF experts have observed, means that those individuals desiring to launder criminal proceeds – unless they already have specialised professional expertise themselves – must turn to the expertise of legal professionals, accountants, financial consultants, and other professionals to aid them in the movement of such proceeds. If one looks at the types of assistance that these professionals may provide, it is apparent that some of these functions are the gateway through which the launderer must pass to achieve his goals. Thus the legal and accounting professionals serve as a sort of 'gatekeeper' since they have the ability to furnish access (knowingly or unwittingly) to the various functions that might help the criminal with funds to move or conceal.*

7. The Report identified money launderers using accountants for such services as: financial advice; audit practice; tax advice and tax structuring; bookkeeping; company formation and administration; trusts; property transactions; and introduction to banks.

### 2. FATF Working Group

8. An FATF Working Group studied various 'Gatekeepers' and reported its findings and recommendations in January 2002. With respect to lawyers the Working Group commented:

*Since the FATF first commenced money laundering methods and techniques on a systematic basis in 1995-96, lawyers have been consistently mentioned in FATF typologies reports as being linked to money laundering schemes and cases.*

Their observations on accountants begins:

*Accounting professionals provide services that can be used and misused by money launderers.*

The Group observed that an ‘*auditor can play an important role as a gatekeeper with regard to the detection and prevention of fraud and money laundering*’. The Report mentioned the International Standards on Auditing (‘ISAs’) published by the International Auditing Practices Committee (‘IAPC’), and in particular ISAs 240 and 250 which deal with ‘*fraud and error*’ and ‘*consideration of laws and regulations in an audit of financial statements*’, respectively. It suggested that the ISAs could be adopted to incorporate a reporting obligation in relation to unusual or suspicious transactions relating to money laundering.

9. The Group’s observations on trust and company service providers stated:

76. *Corporate service providers regularly design structures to ensure that the beneficial owner remains anonymous, and often act as the intermediary between the client and the authorities in the jurisdiction of incorporation...*
78. *Trustees may also play a role in obscuring the identity of the beneficial owner.*

### 3. Revised 40 Recommendations

10. In June 2003 FATF revised and updated its 40 Recommendations. Recommendations 13-16 deal with ‘Reporting of suspicious transactions and compliance’, and require, ‘*Lawyers, notaries, other independent legal professionals and accountants...*’, when they engage in such activities as: buying and selling real estate; managing a client’s money, securities or assets; management of bank, savings or securities accounts; organisation of contributions for the creation, operation or management of companies; or buying and selling business entities, to carry out due diligence on new clients and to keep records for at least five years. Enhanced due diligence procedures must be in place where the client is a ‘Politically Exposed Person’ (‘PEP’) - an individual who is or has been a senior public official, eg politician, government, judicial or military, a senior executive of a state owned

corporation, and important political party officials, as well as individuals who are linked by family or close business association to such officials.

11. These persons are required to report their suspicions about transactions that may involve proceeds of criminal activity, or are related to terrorist financing. However, they are not required to report their suspicions if the relevant information was obtained in circumstances where they are subject to professional secrecy or legal professional privilege. As well, trust and company service providers are subject to the due diligence requirements and the duty to report suspicious transactions.

### C. Hong Kong

12. Hong Kong has been a member of the FATF since 1989. It closely follows and implements the FATF’s 40 recommendations.

#### 1. Money laundering offence

13. Section 25(1) of both Ordinances contains the money laundering offence:

- (1) *Subject to section 25A, a person commits an offence if, knowing or having reasonable grounds to believe that any property in whole or in part directly or indirectly represents any person’s proceeds of an [indictable offence: OSCO] [drug trafficking: DTROP], he deals with that property. (underlining added)*

‘*Dealing*’ is broadly defined in s.2 of both Ordinances and includes: receiving or acquiring property; concealing or disguising property; disposing or converting property; bringing the property into Hong Kong or removing the property from Hong Kong; and using the property to borrow money, or as security. No money laundering offence is committed if a person makes a suspicious property report required by s.25A.

#### 2. Duty to report suspicions

14. The purpose s.25A is to provide Hong Kong law enforcement authorities with timely information about

property that may be connected to crime in order that an investigation of suspected money laundering can commence. Section 25A imposes a statutory duty upon a person to report his knowledge or suspicion that property is connected to an indictable offence [OSCO] or drug trafficking [DTROP], and reads:

- (1) *Where a person knows or suspects that any property -*
- (a) *in whole or in part directly or indirectly represents any person’s proceeds of;*
- (b) *was used in connection with;* or
- (c) *is intended to be used in connection with,*

*[an indictable offence: OSCO] [drug trafficking: DTROP] he shall as soon as it is reasonable for him to do so disclose that knowledge or suspicion, together with any matter on which that knowledge or suspicion is based, to an authorised officer.*

A failure to make a report is a summary offence<sup>2</sup>.

15. Subsection 2 provides the exception to the money laundering offence in s.25(1):

- (2) *If a person who has made a disclosure referred to in subsection (1) does any act in contravention of section 25(1) (whether before or after such disclosure), and the disclosure relates to that act, he does not commit an offence under that section if -*
- (a) *that disclosure is made before he does that act and he does that act with the consent of an authorised officer; or*
- (b) *that disclosure is made*
- (i) *after he does that act;*
- (ii) *on his initiative; and*
- (iii) *as soon as it is reasonable for him to make it.*

16. Subsection 4 is directed at institutions which have compliance officers and procedures which employees must follow in making their reports of suspicious property:

- (4) *In the case of a person who was in employment at the relevant time, this*



*section shall have effect in relation to disclosures to the appropriate person in accordance with the procedure established by his employer for the making of such disclosures as it has effect in relation to disclosures to an authorised officer.*

17. There is some protection to the person making a disclosure. First, it is not treated as a ‘breach of any restriction upon the disclosure of information imposed by contract or by any enactment, rule of conduct or other provision’, and the person is not liable in damages for making a disclosure.<sup>3</sup> Second, a witness in civil or criminal proceedings cannot be asked about whether a disclosure was made, the identity of any person making the disclosure, or answer any question that might reveal these matters.<sup>4</sup>

### 3. Legal professional privilege

18. Prior to recent amendments<sup>5</sup>, s.25A did not expressly or by implication, exclude legal professional privilege (‘LPP’): In Pang Yiu Hung Robert v Commissioner of Police and Another<sup>6</sup>, Hartmann J found:

- (1) Section 25A does not limit nor abrogate common law LPP [para. 81] (this was decided prior to the 2002 amendments coming into operation).

- (2) All persons, including legal practitioners, are subject to the obligations imposed by s.25A. He added:

*... legal practitioners are not to be distinguished from bankers, accountants, stockbrokers, merchants and business people of all kinds: all are the potential victims of money laundering schemes. [para.119]*

- (3) Information relating to solicitors’ trust funds is not covered by LPP, so long as the information does not contain LPP communications. [para.34]
- (4) Information which is not the subject of LPP must be reported. [paras.120-130]

## D. Application of Section 25A

19. Important questions for professionals are:

- (1) What is ‘suspicious property’ or a ‘suspicious transaction’?
- (2) When should a disclosure report be made?
- (3) How is a report made?

### 1. Suspicious Property?

20. Obviously, if a person ‘knows’ that property is the proceeds of crime, then he must report his or her knowledge. Difficulties arise when it comes to ‘suspects’. What does ‘suspects’ mean? In Hussien v Cho Kam<sup>7</sup>, Lord Devlin described ‘suspicion’ as ‘in its ordinary meaning a conjecture or surmise where proof is lacking: “I suspect but I cannot prove.”’ In Queensland Bacon Pty Ltd v Rees<sup>8</sup>, Kitto J defined ‘suspicion’ as:

*A suspicion that something exists is more than a mere idle wondering whether it exists or not; it is a positive feeling of actual apprehension or mistrust; amounting to ‘a slight opinion, but with sufficient evidence.*

The facts of a particular case will determine whether a person knows or suspects that property may be connected with crime.

21. The Law Society’s Circular 97-280 (PA), ‘Money Laundering - Guidelines Notes for Solicitors’ (8 September 1997) lists some indicators of a suspicious transaction at para.C2: unusual settlement requests; unusual instructions; large sums of cash; the secretive client; suspect territory; power of attorney; and suspect personality.
22. A suspicion about the property will often arise from the circumstances of the person connected to the property. The Hong Kong Monetary Authority’s ‘Supplement to the Guideline on Prevention of Money Laundering’ (June 2004), discusses factors to take into account in determining the risk profile of a customer, including: origin of customer; background of

the customer; and being or linked to a PEP.

### 2. When should a disclosure be made?

23. Whenever a person knows or suspects that property falls within s.25A – then he or she must make a report; there is no choice. There is risk if a report is not made: if the person does not make a report when one should have been made, and if the transaction involved a bank, the bank might have made a report which would have alerted the police about the transaction.

### 3. How is a disclosure made?

24. Reports are made to the Joint Financial Intelligence Unit (‘JFIU’) comprising Police and Customs & Excise Department members. Information about the JFIU, including indicators of a suspicious transaction and the procedure for making a disclosure, can be found on its website: <http://www.info.gov.hk/police/jfiu>.

## E. Ethical and Professional issues

25. Section 25A presents ethical and professional issues for every professional who encounters a situation where an obligation to make a report arises. Amongst other things, they may have to consider:
- (1) What is the value of the client’s business if a report is made as opposed to the firm’s reputation if a report is not made? If they don’t make a report and the police subsequently discover this, then they risk being arrested for a s.25A offence or a s.25(1) money laundering offence.
  - (2) If a report is made, can the person continue to act for the client? There is no easy answer. Some assistance may be found in the Law Society’s Circular 97-280 (PA): ‘Money Laundering – Guidance Notes for Solicitors’ (8 September 1997) at para.B3:

*Consequently, where a solicitor knows or suspects that a client is*

*involved in money laundering and a report is made, the solicitor should consider whether the trust and confidentiality necessary between solicitor and client is so affected that the retainer should be terminated. There is no necessary objection to a solicitor continuing to act. Whether or not the solicitor feels able to do so will depend upon all the circumstances. Advice may be sought from the Guidance Committee.*

## F. Responding to the Problem

26. Accountants and company service providers must respond to the risk of being used by money launderers and incorporate anti-money laundering measures into their daily practices by: (a) acknowledging their vulnerability to money laundering; (b) seeking information from law enforcement authorities about suspicious property or transactions and how to report

them; (c) ensuring there is a paper trail of a customer's identification and transactions; (d) implementing a 'know your customer' culture by implementing due diligence procedures for ascertaining details about a client's identity and the nature of his business. But 'knowing your customer' is not enough - they must 'monitor their customer'; (e) implementing internal anti-money laundering guidelines and procedures; (f) educating employees about indicators of money laundering and the application of anti-money laundering guidelines and procedures; and (g) nominating a compliance officer to assess suspicious transactions and reports to law enforcement authorities.

27. Essentially, this requires accountants to be aware of the duty imposed by s. 25A and having measures and procedures in place for making suspicious property reports. In the

end, this is that best protection to the accountant and the profession, and promotes Hong Kong's anti-money laundering laws.

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- 1 Section 25A in both Ordinances. In addition, section 12 of the United Nations (Anti-Terrorism Measures) Ordinance (Cap.575) requires persons to report their suspicions that property may be connected with terrorist activities. This article only discusses the statutory duty under the DTROP and OSCO.
  - 2 Section 25(7) of both Ordinances.
  - 3 Section 25A(3).
  - 4 Section 26(1).
  - 5 In July 2002 the DTROP and OSCO were amended by the Drug Trafficking and Organised Crimes (Amendment) Ordinance 2002, which came into operation in January 2003. Schedules 1 and 2 to the 2002 Ordinance contains amendments to the DTROP and OSCO, respectively, and provide that LPP is not excluded.
  - 6 [2002] 4 HKC 579 (CFI).
  - 7 [1970] AC 942 (HL), at p.948.
  - 8 (1966) 115 CLR 266, at p.303.

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**MICHAEL BLANCHFLOWER, SC**  
**PARKSIDE CHAMBERS**