



Hong Kong

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FSTB CONSULTS ON PROPOSED REGISTRATION REGIME FOR DEALERS IN PRECIOUS METALS AND STONES

On 3 November 2020, Hong Kong's Financial Services and Treasury Bureau (the **FSTB**) published a consultation paper¹ proposing a new two-tier registration regime for dealers in precious metals and stones (**DPMS**) under the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (**AMLO**) with a view to enhancing anti-money laundering (**AML**) and counter-terrorist financing (**CFT**) regulation in Hong Kong. The new regime would require any natural or legal person who wishes to carry on the business of DPMS regulated activities in Hong Kong to register with the Commissioner for Customs and Excise (**C&CE**) under either Category A or Category B. Those who register under Category B will be subject to the AML/CFT obligations under Schedule 2 to the AMLO. The proposed regulated activities will cover not only dealing in precious metals and stones, but also issuing, redeeming and trading certificates or instruments backed by precious metals, stones or products that entitle the holder to the assets (in whole or in part), other than instruments that are regulated under the Securities and Futures Ordinance (**SFO**) as securities, futures contracts, collective investment schemes or authorised structured products.

This proposal is in line with the Recommendations of the Financial Action Task Force (**FATF**), which imposes a range of AML/CFT obligations on financial institutions and designated non-financial businesses and professions (**DNFBPs**), the scope of which includes DPMS. The AMLO was amended in 2018 to extend AML/CFT obligations to legal and accounting professionals, estate agents and trust or company service providers (**TCSPs**), but not to the DPMS sector despite this being covered by the FATF Standards. This was because

the DPMS sector was considered less ready (at the time of the AMLO amendments) than other DNFBP sectors for AML/CFT regulation. The regulation of the DPMS sector was one area which FATF cited as in need of improvement in Hong Kong's September 2019 mutual evaluation² and Hong Kong is expected to have introduced AML/CFT regulation for the DPMS sector by its June 2024 effectiveness assessment.

The consultation paper also outlines a proposal to introduce a new licensing regime for virtual asset exchanges under the AMLO, which is the subject of Charltons' 9 November 2020 newsletter.³

The consultation period closes on 31 January 2021.

Current Hong Kong Regulation of Dealers in Precious Metals and Stones

As of 1 March 2018, further to amendments to the AMLO, DNFBPs have been subject to enhanced customer due diligence and record-keeping obligations. DPMS were not however covered by the amendments to the AMLO given views that the sector "does not pose insurmountable risks in the overall AML/CFT institutional framework in Hong Kong requiring immediate mitigation". This conclusion followed from findings that cash transactions are no longer as common in the sector and that no dealer had (as of 2018) been found linked to or convicted of money laundering offences over the past five years. The FSTB also found that the sector was not "as ready"

¹ https://www.fstb.gov.hk/fsb/ppr/consult/doc/consult_amlo_e.pdf

² www.fatf-gafi.org/publications/mutualevaluations/documents/mer-hong-kong-2019.html

³ <https://www.charltonslaw.com/fstb-consults-on-proposed-licensing-regime-for-virtual-asset-exchanges/>

as other DNFBP sectors in terms of undertaking statutory AML responsibilities and noted that they would consider subjecting DPMS to regulation under the AMLO in the future.⁴ The DPMS sector in Hong Kong is however subject to the suspicious transaction reporting (STR) regime and targeted financial sanctions (TFS) obligations.

In lieu of regulation under the AMLO, an AML/CFT Guideline⁵ was issued to the DPMS sector by the Narcotics Division Security Bureau, which sets out recommended measures, which DPMS are encouraged to implement. Adoption is not however compulsory.

According to Hong Kong's mutual evaluation, FATF concluded that Hong Kong should review and put in place appropriate levels of AML/CFT requirements for the DPMS sector having regard to the money laundering/terrorist-financing risks. This conclusion was based on FATF's findings that the AML/CFT exemption for the DPMS sector was not based on proven low risk, with FATF assessing a medium-low/medium risk, particularly in view of the size of the sector.⁶

This was recognised by the FSTB in the consultation paper, noting that Hong Kong is one of the world's major trading centres in gold and has an active trade in exporting precious stones, particularly diamonds and pearls (HK\$237 billion in 2019). Hong Kong also has a considerable retail sector for jewellery and precious metal accessories, which comprises 2,060 establishments.

FSTB Proposals for Registration of Dealers in Precious Metals and Stones

The FSTB is proposing to introduce a two-tier registration regime for dealers in precious metals and stones under the AMLO. This would require any natural or legal person who wishes to carry on a business in one or more of the designated DPMS regulated activities in Hong Kong, to register under one of two categories (Category A or Category B). The registration regime will be administered by the C&CE, who as the registrar (the **Registrar**) will maintain a register of dealers of precious metals and stones.

a. Scope of Carrying on DPMS Regulated Activity

DPMS Regulated Activity Defined

⁴ https://www.cr.gov.hk/en/publications/docs/consult_eaml-e.pdf

⁵ https://www.nd.gov.hk/pdf/DPMS_Guideline_E.pdf

⁶ www.fatf-gafi.org/media/fatf/documents/reports/mer4/MER-Hong-Kong-2019.pdf

Drawing on FATF's wide scope of persons engaged in DPMS business, the FSTB propose that DPMS regulated activities be defined as carrying on a business in Hong Kong of:

- i) trading in (i.e. selling, offering for sale, purchasing or possessing for sale/resale), importing or exporting precious metals, precious stones or precious products;
- ii) manufacturing, refining, or carrying out any value-adding work (e.g. cutting, polishing etc.) on precious metals, precious stones or precious products;
- iii) issuing, redeeming or trading (as defined) in precious asset-backed instruments; or
- iv) acting as an intermediary for (i), (ii) or (iii) above.

Precious Metals, Precious Stones, Precious Products and Precious-asset-backed Instruments Defined

The FSTB proposes to define precious metals, stones, products and asset-backed instruments as follows:

- i) precious metal – gold, silver, platinum or any other metal in the platinum group in a manufactured or unmanufactured state;
- ii) precious stone – diamond, sapphire, ruby, emerald, jade or pearl;
- iii) precious product – any jewellery, watch, apparel, accessory, ornament or other finished product made up of or containing or having attached to it, any precious metals or precious stones or both, and at least 50% of its value is attributable to the precious metals or precious stones or both; and
- iv) precious-asset-backed instrument – any certificate or instrument backed by one or more precious metals, precious stones or precious products that entitles the holder to such assets (in entirety or in part), but excluding securities, futures contracts, collective investment schemes or authorised structured products regulated under the SFO.

b. Requirements for DPMS Registration

In line with the FATF requirement, the FSTB proposes that DPMS engaging in specified cash transactions (i.e. making or

receiving, in respect of any transaction involving a regulated activity, a payment or payments in cash of at least HK\$120,000 in total, whether executed as a single operation or in multiple operations which appear to be linked) be subject to enhanced AML/CFT obligations, and so propose a two-tier registration regime.

Category A Registration

A person must register under Category A if they do not intend to and will not engage in any specified cash transactions in the course of carrying on a DPMS business. Category A registrants will not be subject to the Schedule 2 AML/CFT obligations and Category A registration will remain valid for so long as the DPMS remains in business, subject to payment of the annual fee.

In order to register under Category A, a person must file an application and submit a valid business registration certificate, addresses of all premises in Hong Kong pertaining to the place of business and a declaration that the registration is obtained for lawful purposes (i.e. to engage in one or more regulated activity).

A Category A registrant will not be subject to any registration conditions other than the requirement to notify the Registrar of any changes in particulars.

Category B Registration

A person must register under Category B if they intend to or may engage in any specified cash transaction in the course of a DPMS business. A Category B registration will be valid for three years and may be renewed where fit-and-proper requirements are met. An applicant who fails to receive registration under Category B may still apply for registration under Category A provided that the applicant does not engage in any specified cash transactions.

In order to register under Category B, an applicant must meet the fit-and-proper test. This will consider whether the applicant (or directors or ultimate owners) has been convicted of any money laundering/terrorist-financing offences or other serious offences; convicted of fraudulent, corrupt or dishonest offences; been the subject of any bankruptcy or liquidation proceedings; or has failed or may fail to comply with AML/CFT and other applicable requirements. The applicant must also submit a valid business registration certificate and addresses of all premises in Hong Kong pertaining to the place of business.

c. Exemptions from the Dealer in Precious Metals and Stones Registration Requirement

The FSTB propose exemptions from the DPMS registration requirement for financial institutions that are already regulated under the AMLO (such as banks, licensed corporations, insurance institutions, money service operators, and stored value facilities) where they conduct regulated activities of DPMS ancillary to their principal business. This exemption will not however apply to other DNFBPs supervised under the AMLO (i.e. legal and accounting professionals, estate agents and TCSPs).

Dealers from other jurisdictions who occasionally visit Hong Kong will also be exempted if the person:

- i) does not ordinarily reside in Hong Kong (in the case of a natural person) or (in the case of a legal person) is incorporated outside Hong Kong and not registered under the Companies Ordinance as a non-Hong Kong company;
- ii) does not have a permanent place of business in Hong Kong; and
- iii) carries out a regulated activity in Hong Kong for no more than a total of 90 calendar days in any given year.

Dealers from other jurisdictions will however be required to file a cash transaction report with the Registrar when engaging in specified cash transactions in Hong Kong within one day of completion of the transaction, and in any event before their departure from Hong Kong.

d. Proposed Powers of the C&CE in Respect of Dealers in Precious Metals and Stones

In respect of Category B registrants, the CE&E will be empowered to supervise their AML/CFT conduct and enforce any registration conditions. This will include powers to enter the registrant's place of business for inspection, investigate non-compliance and request records, documents and other materials, and impose administrative sanctions.

In respect of Category A registrants, the CE&A will be empowered to enter the registrant's place of business and request production of records or documents to ensure they do not engage in specified cash transactions.

e. Proposed Sanctions

The FSTB is proposing the following sanctions.

Conduct/Offence	Proposed Sanctions
<p>Conducting by way of business one or more of the regulated activities without a Category A or B registration;</p> <p>Engaging in a specified cash transaction whilst carrying out any regulated activity without a Category B registration; or</p> <p>Purporting to be a registered DPMS when the person does not have a valid Category A or Category B registration.</p>	<p>Fine at level 6 (HK\$100,000) and six months' imprisonment.</p>
<p>A person makes a statement that is false, deceptive or misleading in a material particular in connection with a registration.</p>	<p>Fine at level 5 (HK\$50,000) and six months' imprisonment.</p>
<p>In the case of a Category B registrant – contravenes the AML/CFT requirements in the AMLO.</p>	<p>Subject to disciplinary proceedings and a range of administrative sanctions (including reprimand, remedial order and pecuniary penalty not exceeding HK\$500,000).</p>

f. 180 Day Grace Period

It is proposed that once the new licensing regime takes effect, DPMS in operation immediately before commencement of the regime will be allowed 180 days to apply for registration and during this transition period, DPMS carrying on a business of regulated activities will be deemed to have been registered until such time when the application is granted.

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