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Hong Kong at laundering's cutting edge

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Hong Kong and Singapore face a money laundering clampdown in the next few months as local banking organisations and regulatory authorities launch rulebooks bringing local rules in line with international standards. These standards are recommended by the Financial Action Task Force (FATF) and the Basel Committee. Some Asian financial institutions will be forced to tighten up their controls.

Local banks, and branches of institutions based in the Asian region can expect tighter scrutiny. But the new rules are expected to have minimal affect on international private banks established in the two jurisdictions who apply systems laid out by their headquarters, say regulators.

Asia 's two leading financial centres are taking different routes to money laundering compliance. Singapore's new rules will be based on risk-based principles, says Tan Sin Liang, a partner with SL Tan and Co, who is advising the Monetary Authority of Singapore (MAS) on its money laundering law. Countries with risk-based systems delegate decisions about the level of due diligence imposed on each transaction or customer to the bank. The local regulators typically police the system with unannounced visits.

The system is devised to assist the banks, says Mr Tan: 'We are throwing the ball into the banks' court. The private bank has to determine for itself whether a customers is a higher or lower risk. It does not have to apply the whole range of due diligence procedures to a low risk customer. That is good for the banks because it means they don't have to apply the same set of rules to every customer. This is the international approach and it is the way forward.'

Risk-based systems rely heavily on the competence of a bank's compliance department, and not all regulators are prepared to trust it. The Hong Kong Monetary Authority (HKMA), for example, has taken the prescriptive approach to money laundering control. This provides a set of rules based on the best practice of Western banks. A group of leading international private banks active in Hong Kong, including Citibank, HSBC, BNP, JP Morgan, DBS and Credit Suisse, advised the HKMA on their rulebook.

Simon Topping, the executive director at the HKMA, says the system will be tough. 'Our rules are very detailed and practical. They say what you really need to do, and these are the checks you must enforce. We want themto help us catch some suspicious transactions. But we don't want to overburden either the banks or the customers.'

Hong Kong's rulebook is also designed to send out a message to investors. 'Our clear and transparent standards will attract business not repel it. People will say Hong Kong is a place where we know it is safe to do business. They will know it is not some dodgy old offshore center or tax haven. We want to be regarded as a smaller version of London or New York. If our new rules prevent a bit of dodgy business coming here because they want banking secrecy, then they can go to another financial center that will take it.'

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Hong Kong likes to be regarded as the region's money laundering policeman and Topping says the territory is widely consulted by other law enforcement authorities in the Region. 'Someone has got to stand up and be counted Someone has to carry the burden, and if it can help the rest of the region develop along the same lines then that's good. We are prepared for a little bit of grief at the outset.'

Singapore 's tough money laundering stance is appreciated by Western bankers. Daniel Truchi, CEO of SG Private Banking (Asia Pacific), says: 'Their rules for money laundering, drug trafficking, and terrorism are very strict. They are comparable in essence to Europe. Hong Kong and Singapore cannot afford to be embroiled in a money laundering scandal if they want to keep the status of being Asia's major offshore centers.' According to Urs Brutsch, global head of clients, ABN AMRO Private Banking, ' Singapore is as strict as Switzerland. They have very tough regulators and an understanding of the Asian business spirit. They want to help the industry grow, because it is clearly one of Singapore's main priorities to make this a global financial center. The country has a good balance of strong regulation, with clear guidelines.' Brutsch argues that the region's retail banks present a greater money laundering risk than its private banks.

Economies east of Hong Kong and Singapore present the greatest money laundering threat to the region. The Financial Action Task Force has blacklisted five countries there, including Indonesia and Philippines, for the inadequacy of their law. Indonesia gives the authorities greater concern than Philippines where efforts are underway to pass anti-money laundering laws, and provide a policing infrastructure. Topping, ' The Philippines have are working to adopt the measures; they are just not quite there yet! So this is an area where the banks have to be very careful, especially when lending to customers from countries on the blacklist.'

Countries in Asia may have money laundering laws on their statute books but many are unable to police them, says Martyn Bridges of UK consultancy Bridges and Partners. 'These countries have the laws, but the further east you go, the less they are applied.' Observers speak of concern about China's level of compliance with international standards, although China is not included on the FATF's blacklist. Bridges says the Region's thriving cash economy presents the regulators with their greatest difficulties. 'The Asian financial sector does not have the same degree of sophistication as that in Europe so people tend to use cash more. They also use cash for other reasons, such as tax evasion. Hopefully they won't take in suitcases to their bank, those days should have gone.'

Regulators expect Indonesia and Philippines to follow in Hong Kong and Singapore's footsteps, and gradually outlaw the cash economy, says Brutsch, 'Ten years ago, a lot more cash used to go around, physical cash as in bank notes. Today we have very few cash transactions. Clients now know that the banks will ask questions if large amounts of cash comes in. If someone comes in with $100,000 in cash it looks very suspicious!'

But cash remains a key part of Japan's economy and that increases the risk of money laundering, says Chizu Nakajima, the director of the Centre for Financial Regulation and Crime at London's Cass Business School. 'People prefer to deal in trade because there is widespread mistrust of the banking system. This increases the opportunities for organised criminals and money launderers.' Nakajima also warns about the resurgence of the Yakuzai organised criminal gangs who present Japan's primary money laundering threat.

Asia's cash economy suits not only its drugs barons who can move their money around without leaving a trace, but also a growing group of terrorists. Monetary authorities now regard them as

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their primary threat, says Tan. 'Terrorist financing is a very big concern. The problem is detecting the terrorist finance because the amounts are very small. That is the challenge. Singapore has passed a whole series of law on terrorism financing, not just money laundering.'

The recent resurgence of terrorism in parts of the region is set to give money laundering initiatives greater momentum. Hong Kong and Singapore's pioneering work has a long way to go.