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Politically Exposed Persons (PEPs) and Customer Due Diligence in Asia –

China, Hong Kong, Singapore and Malaysia

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1. Introduction

Customer Due Diligence in Asia has gained prominence over recent years, with a growing set of regulations that have come into force. International Anti-money laundering standards recommended by the Financial Action Task force (FATF) have provided a framework for member jurisdictions, among them China, Hong Kong, Malaysia and Singapore, to lay out the requirements for the prevention and combat of money laundering and terrorist financing.

While there is no universal definition, Politically Exposed Persons (PEPs) are defined in national legislation in relation to anti-money laundering (AML) laws in most of these countries. PEPs are generally regarded as a high-risk category for conducting business. As such, local legislation requires customer due diligence to be carried out on individuals who are identified as being PEPs. The following paper will first put forth a global definition of the PEP issue. It will then go on to discuss the relevant legislation and the requirements by regulators for identifying PEPs, as well as the due diligence requirements and recommendations for the aforementioned jurisdictions.

Each of the four jurisdictions that will be dealt with have slight regulatory variations in their definition and understanding of PEPs, as well as different investigative and enforcement bodies in place to deal with the risks associated with PEPs. To highlight the differing approaches taken in each country, this paper will examine the legislation in place in each jurisdiction and look at some specific cases in which PEPs have been involved in legal proceedings resulting from allegations of corruption or moneylaundering.

To illustrate the increased prominence of combating corruption and money laundering, it is also worth considering some examples involving stated-owned enterprises (SOEs) and foreign companies doing business in Asia that have been reported in the media. These examples underline the growing importance of the PEP-related issues, prompting banks and companies to optimise processes and improve their compliance management. It is also important to note that high-ranking officials within any of the SOEs are generally considered to be PEPs.

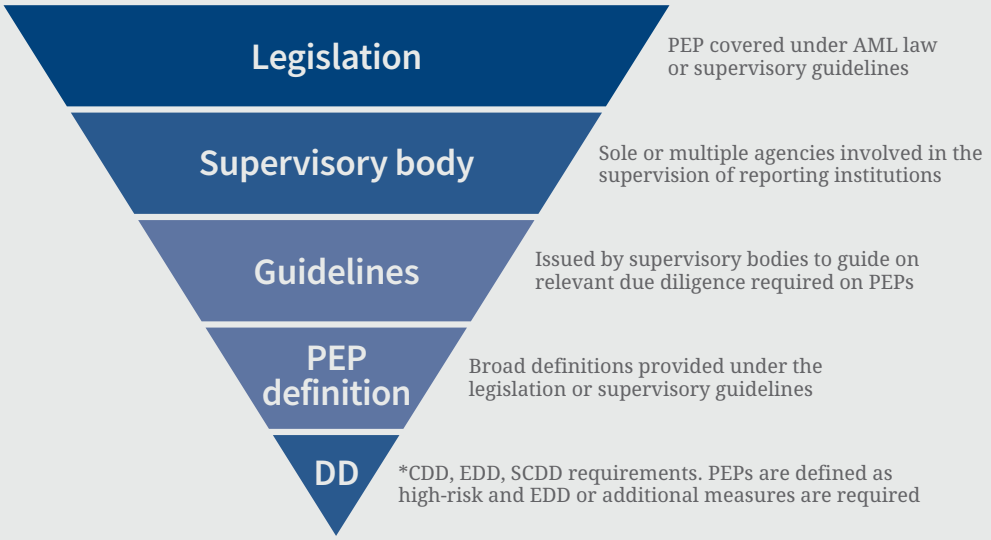
The following report only touches briefly on many relevant issues, but it may serve as an overview of the key issues relevant to customer due diligence requirements in Asia. As said before, the special focus will be on the topic of PEPs. Comparing a selection of four countries in Asia provides insights into the extent to which an anti-corruption outlook has taken foot in this key world region.

2. Global Definition of PEPs

The most widely recognised and internationally binding anti-corruption convention is the United Nations Convention against Corruption (UNCAC) that was established in 2005. Within this convention "public official" or "foreign public official" refers to any "appointed or elected" person holding a legislative, executive, administrative or judicial office and performs a public function, or a function for a public agency or a public enterprise. Interestingly, persons of interest that require identification and screening include people who are entrusted with prominent public functions, and persons who do not have a public function themselves, but who often play an important role when laundering money, such as relatives and business partners of the officials.

Although the UNCAC does not specifically use the term 'politically exposed person,' as the regulations on anti-money laundering and anti-corruption are based on the risk-based approach, the term politically exposed person is synonymous with public official in this context. The term PEP actually goes further than public official, however, as it includes those with formal political power, and those with informal political power, who are still influential political actors.

The FATF Recommendations (2012) define individuals who have been entrusted with a prominent public function as "Politically Exposed Persons", which not only means foreign PEPs but also important functionaries of international organisations. An accompanying interpretive note states that: "Countries are encouraged to extend the requirements of Recommendation 6 to individuals who hold prominent public functions in their own country." The definition also includes family members and close associates of these identified PEPs.



* Customer Due Diligence (CDD); Enhanced Due Diligence (EDD); Simplified Customer Due Diligence (SCDD)

Thorough investigations are required to adequately assess the risk of corruption and money laundering that stems from PEPs. Financial institutions and certain other natural and legal entities must identify the PEPs amongst their customers and business partners, and they must undertake enhanced due diligence regarding these individuals. This includes establishing the "source of wealth and source of funds that are involved in business relationships or transactions with such persons" as well as the ongoing monitoring of those business relationships.

As PEPs are often in the position to illegally favour businesses of which they are themselves beneficial owners, it is important to ascertain what accounts or enterprises they may be beneficial owners of. They may also have direct access to state assets and public funds, which allows for the possibility of theft of public funds. This takes place when state funds are illegally channelled for their own gain or transferred to a trusted acquaintance. Financial institutions that maintain relationships with such individuals are therefore at particularly high risks of money laundering.

3. Country Specific Definitions and Supervisory Bodies

While the most widely accepted definition of PEPs is outlined within the FATF Recommendations and the UNCAC, jurisdictions across the world often have slightly modified versions within their own legislation. Usually they will have used the FATF and UNCAC as the basis for their own definitions, but may have added, omitted or elaborated on certain sections within the definition. Additionally, each jurisdiction has their own supervisory bodies and structures in place to monitor and offer guidance in relation to PEPs.

China

China became a member of FATF in 2007. In the same year, the Chinese Anti-Money Laundering Law came into effect. The main supervisory body is the People's Bank of China, with three sectorial supervisory bodies operating as "Regulatory Commissions" for banking, insurance and securities (CBRC, CIRC and CSRC). China's AML Law does not outline definitions of a domestic or foreign PEP. The FATF Mutual Evaluation Report on China (29 June 2007) critically noted that "the Chinese authorities have not implemented any specific requirements in relation to Politically Exposed Persons (PEPs)." However, it did state that the country had implemented "enhanced measures for transactions to and from China that are conducted by any foreigners."

The following year, apparently in response to the criticism, China issued the Notice of the People's Bank of China on Further Strengthening the Anti-Money Laundering Work, which required financial institutions to define risk levels and provide a definition of a foreign PEP. Financial institutions, it states, should perform enhanced due diligence, if a customer or the beneficiary of a transaction is a foreigner. This is then explained in more detail: "A customer, or a person purporting to act on behalf of a natural person, or a beneficiary of a transaction is a foreigner, or performs an important public function (current or previous), is a head of state, [including] heads

of government, senior politicians, important government, judicial or senior military officials, senior executives of state-owned enterprises, political party officials etc. or family members or close associates." No specific definition for the category of domestic PEPs has been issued. However, FATF later acknowledged that the deficiency had been "substantially addressed" and clarified.

Hong Kong

Hong Kong continued its FATF membership under the name of "Hong Kong, China", since it returned to China in 1997. In Hong Kong's legal system, PEPs are defined under AML/CTF legislations, primarily the Anti-Money Laundering and Counter Terrorist Financing (Financial Institutions) Ordinance (AMLO), which came into effect in 2012. Guidelines produced by several supervisory authorities – the Hong Kong Monetary Authority (HKMA), Securities and Futures Commission, Insurance Authority and Customs and Excise Department – assist in providing more specific and relevant guidelines to the respective industries.

The AMLO definition states that a PEP is an individual who has a prominent function in a place "outside" the People's Republic of China. However, domestic as well as foreign PEPs are included in guidelines from supervisory bodies. For example, the guidelines on Anti-Money Laundering and Counter Terrorist Financing from Hong Kong's currency board (HKMA) and the Office of the Commissioner of Insurance include the definition for domestic PEPs by changing "an individual who is or has been entrusted with a prominent public function in a place outside the People's Republic of China" to "within" the People's Republic of China.

Malaysia

In Malaysia, the definition for PEPs is in line with uniform international standards. Legislation relating to PEPs is covered under the Anti-Money Laundering, Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001 (AMLATF). There are three main supervisory bodies for AMLATF, the central bank (Bank Negara Malaysia), the Securities Commission, and the Labuan Financial Services Authority, regulating the supervision of offshore entities in the special economic zone on the island of Labuan. Each supervisory body has issued specific AML/CFT guidelines.

Where a reporting institution is regulated by multiple bodies, the "more stringent requirements shall apply" according to the Securities Commission guidelines. Enhanced customer due diligence is applicable for a high-risk domestic PEP or highrisk person entrusted with a prominent function by an international organisation. In the case of a PEP that is assessed as low-risk, the reporting institutions can apply the standard CDD measures.

Singapore

In Singapore, the Corruption, Drug, Trafficking, and Other Serious Crimes (Confiscation of Benefits) Act (CDSA) is the main Anti-money laundering legislation, however the Casino Control Act and the Money Lenders Act also cover PEPs and

enhanced due diligence requirements. Singapore's central bank, The Monetary Authority of Singapore (MAS), functions as the sole regulator and supervisory body for AML/CFT over the entire financial sector. It has issued a series of enforceable MAS Notices which provide preventative AML/CFT measures. MAS has recently created a dedicated money-laundering unit, supervisory team, and enforcement department, to strengthen the regulator's ability to tackle money laundering and illicit financing.

PEPs are defined in the notices and guidelines, which outline enhanced due diligence measures on foreign and domestic PEPs. For example, MAS Notice 626 ("Prevention of Money Laundering and Countering the Financing of Terrorism – Banks") outlines the definition of a PEP. In this context, for example, a "family member" means a parent, step-parent, child, step-child, adopted child, spouse, sibling, step-sibling and adopted sibling of the politically exposed person. It is also explained that middle or more junior ranking individuals do not fall in the PEP category. In determining a "close associate," the guidelines suggest that factors such as the level of influence that the PEP has on the person, or the extent of the person's exposure to the PEP, can be considered. The PEP definition in the MAS Notices that were issued to the various financial institutions or class of financial institution, remains consistent with the prior classification.

4. PEP Due Diligence

After establishing definitions and supervisory bodies, each jurisdiction introduced enhanced due diligence measures related to PEPs for corporations and organisations to take when conducting business. The PEP-related due diligence is driven by various factors, including established international standards – Recommendation 6 of the FATF – and national laws on Anti-Money Laundering and Combating Terrorist Financing within each of the four jurisdictions. FATF Recommendation 6 states that financial institutions should have "appropriate risk management systems to determine whether the customer is a politically exposed person" and "obtain senior management approval for establishing business relationships with such customers." The main due diligence measures, aimed at obtaining information and conducting monitoring and review of PEPs, laid out in the guidelines and notices of the supervisory bodies, show that these are generally similar among each of the countries.

China

According to China's AML Law, financial institutions and certain non-financial institutions should establish sound systems of customer identification, customer information identification and transaction record keeping, as well as large value and suspicious transactions reporting, in order to fulfil anti-money laundering obligations. Senior management approval is required to open an account for a senior foreign political official. Financial institutions are required to monitor customers and adjust risk levels based on factors such as their location, occupation and whether they are a foreign PEP. Basic customer information held on high risk customers or accounts should be periodically reviewed at least every six months, drawing attention to the need for on-going due diligence for high risk customers or accounts.

Financial institutions should understand the source of their high risk customers' funds, the use of the funds, their economic status, and their operating status, and strengthen the monitoring and analysis of their financial trading activities. A FATF follow-up report on China in 2012 noted that while the Notice of the People's Bank of China on Further Strengthening the Anti-Money Laundering Work highlighted that understanding the source of funds was a requirement, it has not explicitly included the source of wealth.

Hong Kong

In Hong Kong, the Securities and Futures Commission's guidelines on PEPs elaborate on the statutory definition of a PEP – which only includes individuals entrusted with prominent public function in a place outside of the People's Republic of China – by noting that domestic PEPs may also present, by virtue of positions that they hold, a high risk situation where enhanced due diligence should be applied. It also emphasises that the definition does not exclude sub-national political figures and that the enhanced due diligence measures should also be applied to them. At the minimum, high risk customers should be subjected to an annual review, more frequently if necessary, of their profile to ensure that the CDD information retained remains up-to-date and relevant.

- A summary of main due diligence measures to identify, verify, obtain information and conduct continuous monitoring and review laid out in guidelines and notices by the supervisory bodies show that these are relatively uniform between the countries. Customer background is not explicitly stated in other countries with the exception of China. However, China has not explicitly detailed source of wealth as an EDD measure.
- EDD measures are highlighted in red below.

Due Diligence requirements on PEPs	China	Hong Kong	Malaysia	Singapore
Customer Identification including the establishing the befeficial owner (if applicable)	✓	✓	✓	✓
Customer background	✓			
Business nature	✓	✓	✓	✓
Specified transaction limits	✓	✓	✓	✓
Senior management approval	✓	✓	✓	✓
Review and continuous monitoring	✓	✓	✓	✓
Source of funds	✓	✓	✓	✓
Source of wealth		✓	✓	✓

Malaysia

In Malaysia, referring to PEPs, the supervisory bodies expect that reporting institutions have a risk management system in place to identify PEPs. The Securities Commission's guideline update, in 2014, set new requirements on reporting institutions to conduct enhanced due diligence on foreign PEPs. With regard to a domestic PEP or a person entrusted with a prominent function by an international organisation, the reporting institution is required to take reasonable measures to assess the money-laundering / terrorist-financing risks of the customer. If they are considered to be high-risk, enhanced due diligence must be performed.

Singapore

In Singapore, the central bank (MAS) has issued regulations relating to financial institutions and CDD measures. MAS Notice 626 ("Prevention of Money Laundering and Countering the Financing of Terrorism – Banks") has different sections related to due diligence requirements at various levels: customer due diligence, simplified customer due diligence and enhanced due diligence. The requirements also outline the expectation, in the case of a customer being classified as high-risk, that the customer will undergo enhanced due diligence, including approval from senior management to retain the customer. Guidelines are also clearly stated for identifying legal persons and arrangements.

Interestingly, the Guidelines on MAS Notice 626 provide examples of different approaches that can be taken in scenarios where a financial institution is performing CDD – for example, when a customer is a portfolio asset manager and the identity of underlying investors may, for commercial reasons, be difficult to reveal to the bank. The recommendation is that simplified due diligence should be applied.

On an ongoing basis, the FATF conducts peer reviews of each member to assess levels of implementation of the FATF Recommendations for enhanced PEP-related due diligence. With respect to each of the four jurisdictions, overall compliance is at a level equivalent to "largely compliant." In the case of China, it was stated that the legislation covers most of the required aspects. However, as stated above, one technical deficiency remains because there is no explicit requirement for financial institutions to understand the source of wealth, although they are required to understand the source of funds.

As for Malaysia, the FATF noted that instructions to treat foreign PEPs as 'high risk' are only implicit, which results in a minor weakness. On a further critical note, it was mentioned that there is no required application of ongoing and enhanced CDD provisions for foreign and domestic PEPs in all cases unless higher risk scenarios are identified (Mutual Evaluation Report 2015). In regards to Singapore, the FATF concluded that the AML/CFT requirements applicable to lawyers, including those who provide trust services, have been significantly strengthened and now address the majority of deficiencies identified previously (Mutual Evaluation Second Follow-Up Report 2011).

5. Enforcement and Investigation

Each of the jurisdictions mentioned has an independent anti-corruption and bribery agency that supervises, investigates and enforces breaches of anti-corruption legislation related to public officials. Each agency has varying degrees of judicial power. In some of the jurisdictions they have been employed more readily to enforce the legislation and investigate breaches in conduct relating to PEPs. In the following section the different enforcement agencies and enforcement cultures within the separate jurisdictions are outlined, with some examples highlighted of cases involving PEPs.

China

In China, the Central Commission for Disciplinary Investigation has chief investigative powers within the Criminal Law, including other regulations and anti-corruption campaigns (52 Code of Ethics, "Tigers and Flies", "Eight-Point-Regulation", "Four Winds") governing the behaviour and ethics of public officials/servants and state functionaries, as well as those employed in state-owned entities. The Communist Party of China 52 code of ethics specifies 52 "unacceptable practices" with respect to party officials, including accepting cash or financial instruments as gifts.

The volume of investigations into corruption and the subsequent media coverage is particularly high in China compared to the other countries. Recent anti-corruption campaigns led by President Xi Jinping have resulted in a number of high-profile and senior ranking officials being prosecuted for corruption and bribery offences. However, enforcement figures suggest that prosecutions involving public servants are significantly lower.

One of the highest profile cases as part of China's crackdown on corruption amongst politicians was against the former head of China's security services, Zhou Yongkang[1]. Zhou Yongkang was, as recent as 2012, one of the most senior politicians in the country. The investigation into Yongkang concluded that he had accepted bribes totalling 21 million dollars – as well as committing various other crimes – and was sentenced to life imprisonment.

Hong Kong

In Hong Kong, the Independent Commission Against Corruption investigates violations against the main anti-corruption and bribery legislation, The Prevention of Bribery Ordinance. Convictions in the territory are relatively low; however, there has been a 23 percent increase, from 93 to 114, in the last two years. The Hong Kong Monetary Authority is the organisation that investigates and takes action over violations of the Anti-Money Laundering Ordinance.

Foreign companies can be prosecuted for breaching corruption or money-laundering

1 http://www.cnbc.com/2015/06/11/china-jails-former-security-chief-zhou-for-life.html

rules related to PEPs, as was seen in July 2015 when the Hong Kong Monetary Authority fined State Bank of India (SBI), for breaching anti-money laundering and counter terrorism financing rules[2]. SBI's Hong Kong subsidiary was fined a total of one million dollars for failing to perform sufficient due diligence on some of its corporate customers and for failing to check whether some of its customers were PEPs, although no problem accounts or suspicious transactions were discovered. It was the first time that the Hong Kong Monetary Authority took disciplinary action under Hong Kong's 2012 Anti-Money Laundering Ordinance, as the authority looks to crack down on money-laundering within the city.

Malaysia

Under the Malaysian Corruption Act (2009), the Malaysian Anti-Corruption Commission is responsible for investigating and enforcing corruption offences. However, again, prosecutions are somewhat rare, as the reported number of offenders among public officials has only been 118 in the last two years.

A case that made headlines worldwide in 2015 was the investigation into Prime Minister Najib Razak for allegedly funnelling 700 million dollars from state development fund, 1Malaysia Development Berhad (1MDB), into his personal bank accounts[3]. 1MDB ran up more than 11 billion dollars in debts as a result of dubious investments and has drawn criticism for its lack of transparency. Global investigators believe some of these funds illegally entered Razak's personal bank accounts, although the Malaysian Anti-Corruption Commission claims that its own investigation found that the funds came from donors and not 1MDB.

The fallout from the case has not been restricted to Asia, as The Goldman Sachs Group Inc. is being investigated in the U.S., as of June 2016, for a potential breach of the Bank Secrecy Act, after failing to flag a transaction to a Swiss bank account controlled by 1MDB. Some of the funds ended up in Prime Minister Razak's bank account, according to reports.[4]

Interestingly, in an unrelated case, French prosecutors also launched a formal investigation, in February 2016, into Najib Razak, for allegedly accepting bribes related to a 1.2 billion dollar arms deal between the two countries when he was defence minister[5]. The outcome of this investigation has yet to be reached, however it further intensifies the scrutiny that the Malaysian political system is facing, which could have far reaching consequences past this investigation.

2 http://www.bloomberg.com/news/articles/2015-07-31/hkma-fines-state-bank-of-india-over-moneylaundering-controls

3 http://www.bbc.com/news/world-asia-33439788

4 http://www.reuters.com/article/us-goldman-sachs-1mdb-probe-idUSKCN0YT03P

5 http://www.ft.com/intl/cms/s/0/fab19252-ca85-11e5-be0b-b7ece4e953a0.html#axzz49rrNtd7M

Singapore

The situation in Singapore is similar to that in Hong Kong. The Prevention of Corruption Act (1960) provides, inter alia, that it is an offence for a person to give "any gratification as an inducement to or reward for ( ) any member, officer or servant of a public body doing or forbearing to do anything in respect of any matter or transaction whatsoever, actual or proposed, in which such public body is concerned". However, convictions are rare, in fact, less than 40 people in the public sector were prosecuted under the Prevention of Corruption Act and the Corruption and Drug Trafficking and Other Serious Crimes (Confiscation of Benefits) Act, in 2013 and 2014 combined.

As previously mentioned, MAS is the sole regulator and supervisory body responsible for AML/CFT oversight. MAS is responsible for the enforcement of AML legislation, and has shown a willingness to apply severe punishments for those institutions who are in breach of AML regulations. BSI Bank can attest to this after losing its status as a merchant bank in Singapore in May 2016 for what MAS described as "serious breaches of anti-money laundering requirements, poor management oversight of the bank's operations, and gross misconduct by some of the bank's staff."[6] Additionally, BSI Bank has incurred financial penalties amounting to 13.3 million dollars.

As a subsidiary of the Swiss bank, BSI AG, the proceedings against BSI Bank were initiated by the Swiss Financial Market Supervisory Authority (FINMA). Interestingly, the case against the bank stemmed from business relationships and transactions linked to the Malaysian state development fund 1MDB. In regards to the subsidiary in Singapore, there were widespread control failures, an unacceptable risk culture within the bank, with disregard for compliance and control requirements, and numerous acts of gross misconduct, which led to the shutting down of the bank and the investigation of members of BSI's senior management.

	China	Hong Kong	Malaysia	Singapore
Enforcement and investigation	Violations investigated: 53,085 (2014); 37,000 (2015) Party Members and Cadre processed: 71,748 (2014) People processed: 49,000 including 34,000 who were disciplined by the Party for violations against the Eight Principles (2015) People disciplined by the party: 23,646 (2014) involving Cadres: 68 (of which 30 transferred to judicial organs) (2014); 49,000 (2015) involving Cadres: 90 (of which 42 were transferred to judicial organs) National procuratorial organs investigated for corruption, bribery, wrongdoing: 55,000 (2014); 54,000 (2015) Concluded cases of corruption: 25,000 (2014); 16,000 (2015) Concluded cases of wrongdoing: 5,500 (2014); 4,300 (2015) [Central Commission for Disciplinary investigation]	Persons prosecuted: 101 (2014); 128 (2015) +27% Completed Prosecutions: 113 (2014); 148 (2015) +31% Persons Convicted: 93 (2014); 114 (2015) +23% Persons Cautioned: 7 2014); 11 (2015) +57% Government servants recommended for disciplinary/administrtive action: 26 (2014); 27 (2015) +4% (Period of year is January to June) [Independent Commission Against Corruption]	Corruption offenders Government servant: 84 (2014); 34 (2015) No Detail: 3 (2014); 87 (2015) Public: N/A (2014); 2 (2015) Statutory Body: 5 (2014); 1 (2015) Private: 15 (2014); 3 (2015) Civilian: 107 (2014); 28 (2015) Officer of Public Body: 3 (2014); N/A (2015) [Malaysian Anti-Corruption Commission]	Number of persons prosecuted Public sector employees: 15 (9%) 2013; 20 (12%) 2014 Private sector employees: 163 (91%) 2013; 148 (88%) 2014 [The Corrupt Practices Investigation Bureau]

Data is taken from anti-corruption bodies for two years (2014 and 2015) with the exception of Singapore where data are not available for 2015.

6 http://www.mas.gov.sg/News-and-Publications/Media-Releases/2016/MAS-directs-BSI-Bank-to-shutdown-in-Singapore.aspx

MAS has been quick to act to use this as a basis for large-scale changes to its system for combating money-laundering. Just three weeks after the closing down of BSI, MAS announced the creation of a dedicated money-laundering unit and a supervisory team to assess risks and perform on-site inspections. An enforcement department is also part of the unit, to investigate suspected violations and then take responsibility for enforcement actions. "We will strengthen our supervision of financial institutions' controls to combat money laundering and illicit financing," said MAS managing director Ravi Menon, in a statement. "And we will enhance our enforcement capability to deter poor controls or criminal behavior in the industry."

It is hard to tell whether this penalty, the firmest so far from MAS and the creation of a new specialized unit, will represent the first in a growing trend within the region to clamp down on AML/CFT breaches. Already a hotly debated topic, money-laundering involving PEPs has become highly politicised since the leaking of the now infamous Panama Papers, which exposed companies and individuals hiding money in offshore tax havens. There were more people and companies from China and Hong Kong listed in the database than from anywhere else, with the two jurisdictions combined accounting for nearly one in four of those on the list.[7] This could act as a catalyst for stricter enforcement of AML/CFT regulations and further investigations into the movement of capital from Asia.

Additionally, it should be kept in mind that corporations that are alleged to have committed or have been charged with bribery or attempted bribery may face civil and/or criminal charges imposed by the Foreign Corrupt Practices Act (FCPA) or the UK Bribery Act. Over the past decade, the U.S. Department of Justice and Securities and Exchange Commission have notably stepped up their FCPA enforcement efforts and, with the recent prosecutions under the UK Bribery Act, we are likely to see a further increase in the number of enforcement actions. With regards to the FCPA, of the 12 corporate actions resolved in 2015 almost half of them had a significant Asia-Pacific connection.

As of 31 December 2015, 28 foreign companies are mentioned in on-going FCPA investigations that are related to business activities within China, or with Chinese officials. Some of these companies have already incurred hefty fines resulting from these investigations and reputational damage as a result of the allegations.

One such company, US-based Qualcomm Inc., paid 7.5 million dollars in March 2016 to settle FCPA charges concerning its conduct in China[8]. According to the Securities and Exchange Commission, Qualcomm provided employment and paid internships to family members of Chinese officials to "obtain or retain" business at governmentowned telecom companies in China. The company was also alleged to have provided gifts, travel, and entertainment to try and influence the officials.

7 http://www.scmp.com/news/hong-kong/article/1943463/chinese-dominate-list-people-and-firmshiding-money-tax-havens-panama
8 http://www.fcpablog.com/blog/2016/3/1/qualcomm-settles-fcpa-charges-in-princeling-hiring-casefor.html

6. State-Owned Enterprises

State-owned enterprises (SOEs) can also indicate an apt opportunity to incorporate enhanced due diligence, while the officials of SOEs may very well fit into the definition of a PEP regardless. SOEs have been widespread across all Asian countries since the second half of the 20th century, however, in each jurisdiction SOEs are managed differently, which has resulted in variations in risk levels when dealing with such entities.

In Malaysia, for example, SOEs, now also referred to as Government-Linked Companies (GLC), have undergone a significant transformation since 2004, in an attempt to address poor operational and financial performance. The country established the Putrajaya Committee on GLC High Performance (PCG) as an accountable body to implement and oversee an extensive set of updated policies to be adopted by the SOEs.

Many changes were successfully implemented, including improvements to management structures and the adoption of sound corporate governance practices aimed at increasing efficiency, transparency and accountability. The changes have had a profound influence on Malaysia's SOEs, which have since become significantly more profitable, transforming revenues of the country's 20 largest GLCs from 24 billion in 2004 to 65 billion dollars in 2014[9].

However, although the SOEs in Malaysia are functioning more efficiently, they are still criticised for displaying questionable business practices, particularly related to bribery and unfair competition[10]. Take Malaysia's oil and gas corporation, Petronas, for example, which Transparency International ranks at the bottom of its company scorecard for both anti-corruption and organisational disclosure, and which was recently compelled to launch an anti-corruption initiative.

SOEs in Singapore are generally presented as examples of well-managed and transparent government-linked entities. The feeling is that good political governance has trickled down to the country's SOEs, so that they now display better corporate governance practices. The government's official stance is that SOEs are commercially run and should not be interfered with, however, it does have the Corrupt Practices Investigation Bureau (CPIB) that will investigate any suspicions of corrupt practices within the entities.

It is in China where enhanced due diligence could be considered particularly prudent when dealing with SOEs, as they have recently been subject to a crackdown on corruption and malpractices amongst their upper-management structures.

A large number of businesses in China fall under the various categories of SOEs. Even those that have been privatized are influenced by the state, as state entities often own a minority interest in the privatized companies and exercise varying degrees of control over them. Directors and officers of SOEs are often appointed by the state and may therefore be covered by China's Criminal Law provisions.

9 http://blogs.worldbank.org/eastasiapacific/transforming-state-owned-enterprises-what-othercountries-can-learn-from-Malaysia
10 http://www.gbdinc.org/PDFs/C%20Papers%20SOEs%20April%2025%202012.pdf

Depending on how much ownership and control are held and exerted by the government, everyone at an SOE could be classified as a "foreign official" under the US Foreign Corrupt Practices Act (FCPA). Senior executives are usually chosen by government personnel, not shareholders.

A large proportion of SOEs in China are linked to traditional industries such as steel, coal, shipbuilding and heavy economy, i.e. the old growth model, as SOEs are badly suited to emerging service sectors such as healthcare, technology, education and entertainment. Many of them experience large losses in profits, which has encouraged the government to look at ways to restructure and improve the SOEs. Instead of privatising them, China wants to focus on "strengthening, optimising and enlarging" state firms, which has resulted in a drive towards merging many of the SOEs together. To increase the efficiency of SOEs, the Communist Party has undertaken a campaign to root out corruption within them, which has been partially responsible for the losses that they have been incurring. China launched its sweeping anti-graft campaign in late 2012, with an additional reform to depoliticise the appointment of senior executives.

In December 2015, Premier Li Keqiang reportedly told economic advisers that "for those 'zombie enterprises' with absolute overcapacity, we must ruthlessly bring down the knife." From November 2012 to April 2015, 124 top officials in Chinese SOEs were held on suspicion of corruption, with over 70 of the SOEs' top executives placed under investigation in 2014 alone. Companies in the oil and refinery sector are among those most affected by corruption, while subsidiaries are generally considered riskier than top-level companies. The energy sector, as reported in April 2015, accounts for a quarter of all Chinese SOE officials that were charged as part of the clampdown.

Some of the most recent high-profile officials from the energy industry that have been subject to investigations include Liao Yongyuan and An Wenhua[11]. Liao Yongyuan, vice chairman of PetroChina Ltd and general manager of its parent company CNPC, was placed under investigation in 2015 for committing "serious violations of the law" (often the term used as a euphemism for corruption), while An Wenhua, general manager of PetroChina Tarim Oilfield Company, was placed under investigation at the same time. Just a few months before both managers were placed under investigation, Wang Tianpu, the second-highest ranked official at China's largest oil refiner, China Petrochemical Corporation, also known as Sinopec, was subjected to an investigation on suspicion of "serious violations of discipline and law."[12] These are just a couple of examples, but there are many more, which highlight the sweeping nature of the anti-corruption campaign and its apathy for professional rank.

As part of the drive to strengthen and optimise China's SOEs, many of them have been subject to mergers. As of 2003, the number of companies under control of SASAC (State-owned Assets Supervision and Administration Commission) has fallen from 189 to 103, predominantly as a result of mergers. This number is expected to be further

11 http://www.chinadaily.com.cn/china/2015-06/18/content_21036948.htm;
http://www.chinadaily.com.cn/china/2015-05/05/content_20621017.htm

12 http://www.scmp.com/news/china/policies-politics/article/1778702/quarter-chinese-soe-executivesinvestigated-corruption

reduced to around 40. In 2015, as part of the anti-graft campaign, a group of seven leading international audit firms were chosen by China's government to examine the overseas assets of major SOEs. They found that corruption related to offshore state assets seems to be particularly severe in the merger and acquisition process.

As said before, the Central Commission for Disciplinary Investigation has overriding investigative powers within the Criminal Law and for setting rules and regulations and anti-corruption campaigns, which govern the behaviour and ethics of public officials and state functionaries as well as those employed in SOEs. There are nine separate crimes related to bribery under Chinese Criminal Law, however, these crimes aren't always equivalent to offenses under the Foreign Corrupt Practices Act (FCPA) and the UK Bribery Act.

Problems are often triggered under the Crime of Giving Bribes to a Unit rule that forbids giving rebates to SOEs. The related problems can be avoided by re-checking compliance practices and making sure rebates paid to SOEs strictly adhere to the law. Penalties for bribery offences can range from imprisonment or criminal detention, to fines of varying degrees depending on the case. In especially serious cases, offenders can be sentenced to life imprisonment, as well as having their property confiscated.

In February 2016, China released draft amendments to its Anti-Unfair Competition Law that could reshape how commercial bribery in China is interpreted and enforced. The new rules would more precisely define commercial bribery, including liability for bribes paid through third parties, and vicarious liability for employers for the actions of their employees, while also increasing penalties for commercial bribery.

Li Chengyan, a leading expert and professor of anti-corruption studies at Peking University, underlined that executives in the financial sector have the power to distribute huge amounts of money without being subject to any effective supervisory mechanism. The fact that some foreign banks have recently adopted stricter lending criteria for Chinese SOEs – now asking for collateral and introducing risk assessment procedures when lending to Chinese SOEs – is another visible sign of a new approach.

7. Summary

The white paper explores the due diligence requirements in relation to Politically Exposed Persons (PEPs) under the legislation of China, Hong Kong, Malaysia and Singapore. It has confirmed that PEP-related due diligence in each of the jurisdictions is driven by international standards (Recommendation 6 of the FATF) and national laws on anti-money laundering and combating terrorist financing. The supervisory structure and number of authorities involved in the supervision of compliance of the relevant legislation differs from country to country.

Legislation includes the risk-based approach that forms the basis for the assessment of Politically Exposed Persons and enhanced customer due diligence for high-risk categories such as PEPs. The distinction between foreign and domestic PEPs is drawn in each country, but requirements may vary between them. In China, legislation only requires enhanced due diligence to be conducted on foreign PEPs. Whereas the anti-

money laundering law in Hong Kong excludes domestic PEPs, supervisory guidelines on the other hand include domestic PEPs.

The main due diligence measures, aimed at obtaining information and conducting a review of PEPs, laid out in the guidelines of the supervisory bodies, show that these are generally similar among each of the regulatory framework of the four jurisdictions reviewed. As noted before, overall compliance is assessed by the FATF, and in each of these jurisdictions is seen to be "largely compliant" with the FATF recommendations.

PEPs generally present a higher risk for possible involvement in bribery and corruption. Although enforcement figures seem to be rather low outside of China, especially in relation to the prosecutions of public servants, the local and international media are increasingly reporting about investigations into corrupt practices in the region. Additionally, the recent BSI Bank case in Singapore highlights the severity of the punishments that can be administered to companies judged to have broken anticorruption or anti-money laundering regulations.

China has been clamping down on corruption at the political level and amongst its SOEs, with a large numbers of public officials and the senior management of SOE's subject to vigorous investigations. Singapore has less of a need for a crackdown on corruption, as it has already followed a stringent anti-corruption strategy, which saw it named as the fifth-least corrupt country in the world within Transparency International's "2012 Corruption Perception Index." Corruption in Malaysia is being scrutinised within the public forum as a result of the Najib Razak scandal, which may provoke a response from the Malaysian authorities in the coming years. Overall, with the recent release of the highly publicised Panama Papers, it is likely that any white collar crime in the region will come under increased scrutiny.

The regulatory environment in the jurisdictions assessed considers PEPs to be high risk, especially with regard to financial transactions. All of the four jurisdictions have tightened their anti-money laundering laws, making anti-corruption a central element of new legislation. International corporations and banks doing business in Asia are expected to maintain best practice compliance programmes. The key starting point in this regard is to ensure the use of PEP screening databases to manage the risks attached effectively and to develop appropriate risk mitigation measures and undertake enhanced due diligence as necessary.

In addition, foreign companies and local companies subject to the Foreign Corrupt Practices Act or the UK Bribery Act must also ensure that they are abiding by the rules. These regulations have also seen increased scrutiny in the Asian region which has resulted in a growing number of corporations being implicated in on-going FCPA investigations in relation to their business activities in China, resulting in large fines for some of the companies involved, as well as damage to their reputation.

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