aml

From: [redacted]@barfoot.co.nz>
Sent: Friday, 3 December 2021 11:25 am
To: aml
Subject: Submission: AML/CFT Consultation Document Oct 2021
Attachments: AMLCFT submission final.pdf

Please find attached our submission in respect of the above consultation document.

Thank you for the opportunity and we look forward to engaging with you further in the coming months.
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[redacted]
SENIOR LEGAL COUNSEL
[redacted]

Administration 09 307 6300
34 Shortland Street, Auckland Central

Starship
Five Star Partner

BARFOOT & THOMPSON
LICENSED REAA 2008

3 December 2021

AML/CFT Consultation Team
Ministry of Justice
SX 10088
Wellington 6140

BY EMAIL: aml@justice.govt.nz

SUBMISSION: REVIEW OF THE AML/CFT ACT CONSULTATION DOCUMENT - OCT 2021

Thank you for the opportunity to submit on the Review of the AML/CFT Act Consultation Document, October 2021 (**Consultation Document**).

Barfoot & Thompson is New Zealand's largest, family owned real estate agency and operates almost exclusively in the Auckland/Northland region. We operate 78 branches providing a full range of real estate services and engage, on a contract basis, 99 licensed branch managers and 1700 licensed salespersons.

Under the AML/CFT Act, Barfoot & Thompson is captured as a designated non-financial business or profession and as such is supervised by the Department of Internal Affairs (DIA). We take our AML/CFT obligations seriously and are committed to helping prevent money laundering and terrorist financing activities occurring through the vehicle of real estate.

This submission addresses questions 4.6 - 4.8 of the Consultation Document, before commenting broadly on the efficacy of the current AML/CFT regime.

We look forward to participating in your real estate industry specific consultation process, which we understand will take place in 2022.

4.6 Should we amend the existing regulations to require real estate agents to conduct CDD on both the purchaser and vendor?

Barfoot & Thompson does not support amending the regulations to require real estate agents to conduct CDD on purchasers. Our current view is that the expected compliance costs associated with completing CDD on purchasers would be disproportionate, particularly given that other reporting entities (e.g. lawyers and banks) already gather information on purchasers.

We seek clarity from the Ministry of Justice (MOJ) and DIA as to:

a. the precise ML/FT activity/risk that real estate agents could identify by completing CDD on purchasers, that other reporting entities cannot; and

b. how completing CDD on purchasers would contribute to a reduction in ML/TF activity in New Zealand and to what extent.

We look forward to obtaining your clarification on these matters during MOJs/DIAs industry consultation next year.

In the meantime, based on the following broad statement on page 49 of the Consultation Document, we assume that the real estate risk/activity with which MOJ and DIA is concerned is in relation to the payment of deposits to agents by purchasers:

> *…it is typically the purchaser, rather than the vendor, who represents the main threat of money laundering or terrorism financing in real estate transactions. The current approach may also provide limited visibility over who initially pays the deposit, especially where they do not end up being the ultimate owner of the property.*

Regarding the above statement, we note that "the ultimate owner of the property" is determined through a process managed by lawyers, not real estate agents. Purchasers can nominate a different person or entity (the nominee) to settle the purchase but this occurs at (or close to) the settlement date and is picked up by the purchaser's/nominee's and vendor's lawyers. Agents have no visibility over the nomination process.

On the matter of deposits, real estate agents receive deposit monies from purchasers via the purchaser's bank. The amount of these deposits generally range from 5-10% of the purchase price. The remaining 90-95% of the purchase price changes hands at settlement, which is a process managed entirely by the party's lawyers and usually with the involvement of the purchaser's bank. The additional compliance burden for real estate agents in completing CDD on all purchasers appears to outweigh the perceived ML/FT risk such a measure might mitigate (the risk has not been clearly articulated or quantified in relation to deposits).

Furthermore, agents are already required to conduct CDD on purchasers where a purchaser requests that their deposit be refunded/transferred to someone other than the purchaser. In our view, this existing requirement already ensures that CDD is completed by agents on purchasers in relation to deposit related activity that is high risk.

Before addressing question 4.7 of the Consultation Document, we comment on the following statement on page 49:

> *The current requirements for real estate agents when conducting CDD are not in line with the FATF standards. The FATF requires real estate agents to conduct CDD on both the vendors and purchasers of the property.*

The FAFT guidance is generic and may not allow for the unique ML/FT protections that already exist by default within New Zealand's real estate and conveyancing processes. For example:

a. In New Zealand, agreements for the sale and purchase of land must be in writing. Most property sales are completed using an industry standard sale and purchase agreement, which has both real estate and legal industry endorsement. The agreement captures the legal name of the purchaser and these details must be the same as the details that appear on the certificate of title at the time of transfer, unless the purchaser engages their lawyer to alter the details (e.g. through the nomination process).

b. Property transfers must be completed by lawyers via the New Zealand Government's centralised, Landonline e-dealing platform. Use of this platform first requires lawyers to ensure that their client (be it a vendor or a purchaser) are correctly identified using prescribed forms (i.e. Client Authority and Instruction forms).

4.7 (a) What challenges do you anticipate would occur if this was required?

There is no practical point at which an agent can complete CDD on a purchaser. We expand on this statement below.

The New Zealand real estate model is based on inviting a number of prospective purchasers to express an interest in a property. Agents often deal with a significant number of prospective purchasers for a single property (sometimes hundreds), each of whom have the intention of fulfilling the transaction. It is therefore impractical for CDD to be carried out on all interested parties. The administrative, compliance and cost burdens associated with completing CDD on all prospective purchasers appears to far outweigh any perceived or actual reduction in ML/FT risk.

The alternative is for CDD to be completed on a purchaser at the time they enter into a sale and purchase agreement. This is also impractical for the following reasons:

a. **Agreement entered into via the standard negotiation process**:

   If CDD cannot be completed, the agreement will fall over. Other interested parties will likely have bought elsewhere and the sale process will have been undermined. Costs incurred by vendors to market their property, which can be significant, will have been wasted.

   Agreements include specific timeframes for fulfilling conditions and completing settlement. It is highly unlikely that purchasers would incur the costs (legal and other) associated with fulfilling conditions until CDD is completed. If CDD is delayed, either party could potentially avoid the contract for non-fulfilment of conditions. Again, the sale process would be undermined.

   If CDD is delayed or unable to be completed resulting in an agreement falling over, agents will (rightly or wrongly) be exposed to claims from one or both parties. Frivolous claims still require significant time and resource investment to resolve.

b. **Auctions:**

   Barfoot & Thompson holds approximately 275 auctions per week with multiple bidders per property. The property is sold on the fall of the hammer to the successful bidder, who then pays their deposit. Accordingly, to avoid the issues noted in paragraph (a) above, CDD would need to be completed on every bidder in advance. This is despite the reality that only one bidder will be successful. This would create an enormous administrative and compliance burden on real estate agents, which appears to far outweighs any actual or perceived reduction in ML/FT risk that might be achieved.

c. **Tenders:**

   The tender process invites multiple prospective purchasers to put forward their best offer on a property. The vendor receives all tenders at once and chooses which offer to accept/negotiate. As would be the situation with auctions, CDD would need to be completed on every offeror in advance despite the reality that only one offeror will be successful. Once again, this would impose a disproportionate compliance burden on real estate agents.

4.7 (b) How might these be addressed?

We have been unable to identify any practical solutions to the issues raised above in relation to the timing of conducting CDD on a purchaser, that do not involve undermining the sale and purchase process to the detriment of vendors and purchasers.

However, one solution that would significantly reduce the administrative and cost burdens associated with conducting CDD would be for the Government to endorse a centralised identification/ CDD system. A secure, centralised identification system that could be relied on by multiple reporting entities to

complete CDD (rather than having each reporting entity collect the same CDD information on the same people at multiple points throughout a transaction) would significantly reduce compliance costs.

4.7 (c) What do you estimate would be the costs of the change?

Each year Barfoot & Thompson outlays nearly $1 million in direct wage and salary costs (excluding branch manager's time) for AML management and administration. Additionally, on an annual basis, we expend approximately $180,000 in compliance software costs, $35,000 on audit and assessment and more than $30,000 in direct training costs.

Between January and November 2021, Barfoot & Thompson onboarded approximately 25,000 vendors (individuals, trusts and companies). We would expect the number of onboards to double if we were required to complete CDD on purchasers. As correctly noted at page 49 of the Consultation Document, "*requiring real estate agents to conduct CDD on both parties potentially doubles the compliance costs associated with CDD*".

4.8 When is the appropriate time for CDD on the vendor and purchaser to be conducted in real estate transactions?

The cost and disruption associated with a change to the timing of vendor CDD could be significant. Accordingly, any change to the current timing (which is well understood by the industry and firmly embedded in processes) needs to be carefully considered. We look forward to engaging in this discussion with MOJ and DIA during the industry consultation next year.

General Comments

AML legal framework

a. The current discretionary risk-based approach provides reporting entities with the ability to make informed judgements in relation to the AML risk that customers may bring to a real estate transaction. That risk can be assessed alongside a number of pre-prescribed criteria that meet the over-arching need to have knowledge of the client's business structure, source of wealth and source of funds.

   Gaining the knowledge at the entry level of a relationship with the customer enables an early assessment of potential risk.

   In our view, increased compliance obligations would appear to add little value and disproportionately increase compliance costs. AML/CFT compliance costs are currently largely absorbed by our agency. However, if compliance costs were to increase significantly, it may become necessary to pass on these costs to vendors and purchasers.

Enforcement and penalty

b. Currently the Act prescribes penalties of $100,000/$200,000 for an individual and $1 million/$2 million in the case of a body corporate or partnerships that have engaged in conduct that constitutes a civil liability act. The review document suggests that there could be a widening of AML/CFT penalties. It is the view of this agency that the current penalties are at level that is sufficient to ensure full compliance at all levels.

On-going relationships

c. In general terms in a real estate environment, a customer's relationship with a real estate agency is for the one specific purpose of transacting the sale of the customer's property. When that

objective has been achieved, the relationship is terminated until the next time the customer engages an agent to act for them; this could well be a lengthy period. There is no enduring and on-going relationship between a real estate agent and customer as there may be with other reporting entities.

On this basis it would be appropriate to mandate a specific time period across the industry after which, if a customer again engages an agency, it is necessary to obtain new/fresh due diligence documentation. The counter that this would create unnecessary work or duplication is not supported and is negated by the overarching requirement of the Act to ensure that a reporting entity's on-boarding processes ensure that a customer's identity is clearly established.

Suspicious Activity Reporting

d. The current prescriptive nature of the Act in regard to the processing of suspicious activity/transaction reports is at variance to the remainder of the Act that allows a reporting entity to assess AML/CFT risk. The report process itself is unwieldy, confusing, and difficult to understand and follow through and is totally process driven.

   All reporting entities and all supervisors would be better served by a complete review of the current process driven reporting method with a view to replacing it with a simplified system that is driven by a focus on risk assessment, rather than form.

Customer due diligence

e. Customer: Insistence on the use of the word 'customer' to cover both client and customer is confusing. While from a real estate perspective there has had to have been an acceptance that a 'customer' is actually a client (and not a customer) there remain instances were clarity is required to ascertain the correct nature of the relationship.

   This confusion could be eliminated in real estate AML transactions by using the far simpler and clearly understood terminology of seller and purchaser. It is noted that throughout the consultation document the words seller and purchaser are used consistently rather than customer.

f. Address verification: The Act does not specify that a customer's address needs to be verified; this requirement has been established as a best practice under DIA AML/CFT guidelines. It should be recognised that a customer's address is an integral part of the AML on-boarding process and changes made to reflect that.

Thank you again for the opportunity to submit on the Consultation Document and we look forward to engaging with your further in 2022.

Yours sincerely

Managing Director

General Counsel