aml

From: [redacted]@buddlefindlay.com>
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To: aml
Subject: Review of the AML/CFT Act - Consultation Document - Submission
Attachments: AML_CFT consultation submission(62196126.1).pdf

Please find attached,

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17 December 2021

To
AML/CFT Act consultation team
Ministry of Justice
DX Box SX 10088, Wellington, New Zealand

From
[redacted]

By email
aml@justice.govt.nz

AML/CFT Act consultation

1. Buddle Findlay welcomes the opportunity to make submissions on the Review of the AML/CFT Act Consultation Document (the "**Consultation Paper**"). While we broadly support the reforms proposed in the Consultation Paper, we have identified certain areas (using the question numbering from the Consultation Paper) where we disagree with the reforms proposed, or where we believe further consideration is required.

Licensing and registration (1.52 – 1.54)

2. In the Consultation Paper, the Ministry of Justice (the "**Ministry**") has indicated that it wishes to explore the creation of a new anti-money laundering and counter the financing of terrorism ("**AML/CFT**") registration regime.

3. In our view, there is no need for a new, AML/CFT-specific registration regime. Many reporting entities are already registered and supervised in relation to their business activities under other regimes. Financial institutions are already potentially subject to multiple regimes (as registered banks, licensed NBDTs or insurers, certified consumer credit lenders, and as registered financial service providers) and many DNFBPs are separately regulated by professional bodies (for example, Buddle Findlay as a law firm is supervised by the New Zealand Law Society). In addition, reporting entities are already obliged to notify the relevant AML/CFT supervisor if they are a reporting entity under the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (the "**Act**"), and the three supervisors already maintain publicly accessible lists of reporting entities which they supervise.

4. A new, specific registration scheme will increase the cost of compliance for reporting entities – as it is likely that reporting entities will be asked to bear the cost of complying with, establishing, and maintaining any registration scheme – without providing any tangible value. Since reporting entities are already required to notify themselves to the relevant AML supervisor, the addition of a formal register is unlikely to have a significant positive impact. Reporting entities who are currently unaware of, or non-compliant with, their AML/CFT obligations under the Act would similarly be unlikely to comply with any requirement to be formally registered under a new registration regime.

5. In the Consultation Paper, the Ministry suggests that the new registration scheme may be warranted because some high-risk businesses in specific industries (such as money remitters,

virtual asset service providers, and trust and company service providers) are only subject to limited fit-and-proper checks. In our view, if there is a particular need to impose such checks on directors and senior managers of businesses in specific industries, then that should be addressed through specific regulations for those industries. The focus and purpose of the Act is the detection and prevention of money laundering and the financing of terrorism, not whether directors and managers are fit-and-proper persons to carry on a particular business in a particular industry.

Ordinary Course of Business (2.1 – 2.3)

6. The Consultation Paper proposes that the term "ordinary" could be removed from the definition of a designated non-financial business or profession ("**DNFBP**"). This would mean that businesses would have to undertake risk assessments, appoint a compliance officer, develop full compliance programmes, file annual reports, report suspicious activity and otherwise comply with all obligations under the Act, even where the only captured activity by the business is highly infrequent or one-off. This would involve considerable and disproportionate compliance costs.

7. In our view, businesses are themselves best placed to determine what is in the "ordinary course" of their business (notwithstanding the absence of a legal definition or test in the Act) and accordingly the term "ordinary" should remain in the definition. The term in our view correctly reflects the focus of the Act on ordinary business activity undertaken by a reporting entity which, from an AML/CFT risk perspective, is likely to be the activity (rather than unusual or one-off activity) that attracts criminals to use a reporting entity for placement, layering and integration purposes.

8. If reference to "ordinary" is removed, the cost of compliance is likely to be prohibitive and will outweigh any benefit obtained by forcing compliance across a wider range of reporting entities. The Ministry suggests the costs involved with removing the term "ordinary" could be reduced by exempting reporting entities from certain requirements where only one-off activities are undertaken. However, adding exemptions is likely to add significant complexity (which runs counter to the Ministry's aim of reducing confusion and complexity), as businesses who would not otherwise consider themselves subject to the Act will need to determine (and seek advice) as to when and how exemptions will apply to their business, what conditions to the exemptions they may need to comply with, and what other residual obligations under the Act they may remain subject to. Increasing the scope of reporting entities which are subject to the Act, but otherwise partially exempt from certain obligations, will also add to the burden borne by AML supervisors by increasing (without any real benefit) the number of entities which the AML supervisors need to supervise.

Managing client funds (2.8 – 2.9)

9. The Consultation Paper suggests the reference to "professional fees" in the definition of the DNFBP activity of "managing client funds" should be clarified. In our view, if the reference is to be clarified, "professional fees" should include reimbursement or recovery of third party costs where the reporting entity has incurred those costs in the ordinary course of providing its services to its customer. This would exclude third party fees which the customer (rather than the reporting entity) is liable to pay to a third party.

10. Allowing for the recovery of third-party costs incurred in the ordinary course of providing services does not, in our view, represent a significant money laundering risk. These costs could be internalised and recovered through a reporting entity's own fees to its customer, and so it should not matter (from an AML/CFT risk perspective) if those costs are separately itemised from the reporting entities' own fees when invoiced to the customer. This is consistent with the existing exemption in regulation 24AB of the Anti-Money Laundering and Countering Financing of Terrorism (Exemptions) Regulations 2011.

Engaging in or giving instructions (2.10 – 2.11)

11. The Consultation Paper suggests the term "engaging in" certain activities (which is used in relation to certain captured activities performed by DNFBPs) could be changed to "assisting a customer to prepare for" certain activities. In our view, this would overly broaden the scope of activities which are captured to include purely advisory or ancillary activities that do not present an AML/CFT risk, and would create uncertainty as to where the definitional boundary lies.

12. The phrase "engaging in or giving instructions" is used in relation to specific activities that DNFBPs might do, namely (i) conveyancing, (ii) land transfers (iii) transactions as defined in the Real Estate Agents Act 2008, and (iv) transactions (in general, making payments) as defined in the Act. As currently defined, the meaning of the phrase is clear – to constitute captured activity under the Act, the reporting entity must be either engaging in (in other words, undertaking) that activity itself for its customer, or giving instructions to another on behalf of its customer to do so. Expanding the meaning of that phrase to include "assisting a customer to prepare for" those activities could include a range of indirect advisory and other activities which are not – and should not be – captured under the Act. This would increase uncertainty as to what is captured, increase compliance costs, and risk capturing activities which are not intended to be caught under the Act.

Acting as a trustee or nominee (2.49 – 2.51)

13. The Consultation Paper raises the possibility of whether persons acting as a trustee or nominee should be exempt from being reporting entities or subject to AML/CFT obligations in certain situations, such as where the nominee or trustee company is a wholly owned subsidiary of a parent DNFPB. We would support a new regulatory exemption to that effect, provided that the parent DNFPB remains responsible for complying with all AML/CFT obligations (as if the customers of the nominee or trustee company were customers of the parent DNFPB). Such an exemption would mean that there will no longer be unnecessary duplication of compliance costs and resources, but AML/CFT obligations will still be undertaken by the DNFPB parent.

Territorial scope (2.56 – 2.57)

14. In our view, it would be preferable for the territorial scope of the Act to be clearly set out in the Act, rather than having to rely on guidance issued by the AML supervisors.

15. The current test under the guidance produced by the AML supervisors is vague and uncertain in application, relying as it does on whether an entity is "carrying on business in New Zealand", which is said to "imply" a place of business in New Zealand, and is "likely to include" New Zealand staff or infrastructure. A clear territorial scope set out in the Act would ameliorate this problem. The criteria

used in the Act should, we would suggest, align with the criteria used in the Financial Service Providers (Registration and Dispute Resolution) Act 2008 where the reporting entities are financial institutions.

Definition of a customer (4.2 – 4.5)

16. A more prescriptive approach to the definition of a customer would be helpful in situations where funds are received or held by a DNFBP, either as a stakeholder or escrow agent, for multiple parties in relation to a transaction. Customer due diligence in those circumstances should not be required for parties which, but for the fact that funds are held for their joint benefit under a stakeholder or escrow arrangement, would not otherwise be a customer of the DNFBP.

Conducting customer due diligence in all suspicious circumstances (4.11 – 4.13)

17. The Consultation Paper suggests amending the Act so that CDD is required in all suspicious circumstances, irrespective of whether the reporting entity has a business relationship, or is engaged in an occasional transaction, with the customer.

18. In our view, it is unreasonable and impractical to require a reporting entity to obtain identity information from an entity that it has no business connection with. Similarly, it is not reasonable to expect that an entity with no connection to the reporting entity would agree to provide that information. Moreover, we expect that asking for this information would invariably lead to tipping off – if a reporting entity with no relationship to a third party entity asks for identity information, that would likely arouse the suspicion of that third party.

Managing funds in trust accounts (4.14 – 4.17)

19. The Consultation Paper suggests introducing further requirements and controls in relation to the use of trust accounts.

20. In our view, such changes would be unnecessary and ignores the stringent regulatory controls and audit requirements that the operation of law firm trust accounts are already subject to (under the Lawyers and Conveyancers Act (Trust Account) Regulations 2008). The use of trust accounts does not present any specific or unique money laundering vulnerabilities which are not already addressed by the requirement under the Act to undertake CDD in connection with the management of client funds, and to comply with wire transfer and prescribed reporting obligations.

21. Furthermore, the introduction of additional requirements and controls could conflict with a firm's fiduciary or professional obligations in relation to the operation of a trust account. For example, rule 10.5.2 of the Lawyers and Conveyancers Act (Lawyers: Conduct and Client Care) Rules 2008 requires that lawyers who receive funds on terms requiring the lawyer to hold the funds in a trust account as a stakeholder must adhere strictly to those terms and disburse those funds only accordance with them. This could conflict with the suggestion made in the Consultation Paper that law firms must conduct CDD on third parties before refunding money to them.

Person on whose behalf a transaction is conducted (4.35 – 4.37)

22. The Consultation Paper proposes clarifying, in regulations, what is meant by the term "person on whose behalf a transaction is conducted" (a "**POWBATIC**"). We would support this, given the

confusion as to how the POWBATIC term has been interpreted. However, the specified managing intermediaries ("SMI") exemption set out in Part 6 of the Anti-Money Laundering and Countering Financing of Terrorism (Class Exemptions) Notice 2018 should be retained, even where the POWBATIC definition is clarified. The exemption is particularly relevant to transactions involving a POWBATIC as it allows reporting entities to rely on confirmations made by their customers (where the customer is itself a reporting entity). Removing this exemption would mean that reporting entities may have to determine, on a case-by-case basis, whether their customer's underlying customers exert "indirect ownership or control" over the reporting entity's customer, which would appear to be impractical.

Conducting simplified CDD on all persons acting on behalf of large organisations (4.56 – 4.57)

23. The Consultation Paper suggests removing the requirement to verify the identity and authority of a person acting on behalf a customer, where that customer is a large organisation to which the simplified CDD processes of the Act would apply. We support that proposal, and suggest that it should not be necessary to obtain identity information verifying the name and date of birth of a person acting on behalf of such a customer where a senior manager within the customer is able to provide the reporting entity with a list of persons delegated to act on its behalf.

Mandatory enhanced CDD for all trusts (4.58 – 4.60)

24. The Consultation Paper proposes removing the requirement that enhanced CDD be conducted for all trusts. Instead, enhanced CDD would only be required in high-risk situations. In our view, this is a sensible change and appropriate given the risk-based approach to regulation under the Act.

25. Although some trust structures can give rise to money laundering and financing of terrorism risks, not all trusts are structured in this way. It would be preferable to remove the mandatory requirement and replace it with guidance as to when a transaction involving a trust should be considered high-risk. This could include situations where there is no commercial justification for the trust, or the trust is being used to disguise or anonymise ownership. Only in these situations – where the structure of the trust is such that it can be considered high risk – should enhanced CDD be required.

Conducting CDD on existing (pre-Act) customers (4.71)

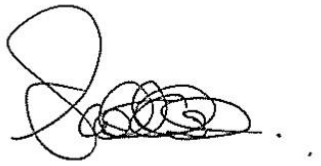
26. The Consultation Paper identifies a number of possible changes to the circumstances in which CDD must be conducted on existing customers of a reporting entity, when the reporting entity became subject to the Act.

27. The Consultation Paper suggests changing the trigger from an "and" to an "or", such that reporting entities would have to conduct CDD on existing customers whenever the reporting entity believes they have insufficient information or there is a material change in the nature of the purpose of the business relationship with the customer. We would suggest retaining the current wording, which effectively requires there to have been a material change in business relationship, at which point the reporting entity can check to determine whether the information it holds is sufficient. If the word "and" is removed, reporting entities will be obliged to check whether information is sufficient (that is

to say, that identity details have not changed) at all times. This will increase the cost of compliance for reporting entities.

28. The Consultation Paper also suggests lowering the threshold from a "material change" in the nature or purpose of the business relationship, to simply a "change" in the nature or purpose. We expect that this is likely to increase confusion as to when CDD is required, and will lead to reporting entities conducting unnecessary CDD. The removal of the term "material" would suggest to reporting entities that CDD would have to be conducted any time there is a change (however insignificant from a risk perspective) to that purpose or nature. This will increase the cost of compliance, without adding any real benefit.

Yours faithfully
Buddle Findlay



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