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Sent: Wednesday, 22 December 2021 10:08 am
To: Kokay, Nick; aml
Cc: [REDACTED]
Subject: RE: RBNZ submission on Statutory Review consultation document
Attachments: RBNZ submission to AMLCFT Statutory Review_final 22Dec 2021.pdf

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Hi Nick

Please find attached the RBNZ Submission on the AML/CFT Statutory review. The document is encrypted, I will send the password separately.

Apologies for the delay, it took us longer time to get the internal sign off at this time of the year.

Hope you have a nice summer break, we look forward to continuing to work with you on this in the new year.

Thanks again for the extension.

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Subject: RE: RBNZ submission on Statutory Review consultation document

Kia ora [REDACTED],

Absolutely fine – take all the time you need!

Ngā mihi,

Nick



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Subject: RBNZ submission on Statutory Review consultation document

Kia ora Nick,
 RBNZ is intending to provide a concise submission on the consultation document. Due to the interest, it will include comments from different areas with RBNZ e.g. Cash&Money and Pacific Remittance Project

However, I would like to formally request a submission extension on behalf of RBNZ until 17th December 2021. It is likely we will get in earlier, but I just want to make sure we have a contingency.

Thanks,

[REDACTED]

[REDACTED]

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Thank you.

Submission to the Ministry of Justice on the Consultation document: Review of the AML/CFT Act

Reserve Bank of New Zealand - Te Pūtea Matua

22 December 2021



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About RBNZ

1. The Reserve Bank of New Zealand - Te Pūtea Matua ('**RBNZ**') is New Zealand's central bank that regulates banks, insurers, non-bank deposit takers (including finance companies that take deposits from the public, building societies and credit unions), and financial market infrastructures for the purpose of promoting the maintenance of a sound and efficient financial system.
2. This submission has been prepared by RBNZ's Anti-Money Laundering and Countering Financing of Terrorism ('**AML/CFT**') Supervision team, Money and Cash department, and the Pacific Remittance Project team.
3. The AML/CFT Supervision team supervises New Zealand registered banks, non-bank deposit takers, life insurers, and relevant designated business group members under the AML/CFT Act 2009 ('**the AML/CFT Act**').
4. The Money and Cash department is responsible for the production and distribution of bank notes and coins, providing stewardship of the cash system so that it meets the needs of New Zealanders, and evaluating the broader policy issues associated with the future of money in New Zealand, including any potential case for a central bank digital currency.
5. RBNZ's Pacific Remittance Project was established in 2019 with the aim of enhancing access to, and reducing the costs of remittances to the Pacific. The project is currently exploring a range of initiatives including ongoing information gathering exercises, policy and legislative changes, and the development of a regional electronic know-your-customer facility. This work will help address some of the underlying factors contributing to the withdrawal of correspondent banking relationships.
6. RBNZ welcomes the opportunity to provide feedback to the Ministry of Justice ('**MOJ**') on its consultation document "Review of the AML/CFT Act".
7. RBNZ has chosen to provide comments and feedback to only specific parts of the consultation document, not all. We have structured our submission to mirror the structure of the consultation document.
8. If you would like to discuss any aspect of the submission, please contact:

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Part 1. Institutional arrangements and stewardship

Purpose of the AML/CFT Act

Actively preventing money laundering and terrorism financing

9. RBNZ supports a purpose of the AML/CFT Act extending beyond 'detecting and deterring' money laundering and terrorism financing ('ML/TF') to also include preventing ML/TF. However, RBNZ considers this extension would need to be carefully balanced to avoid increasing instances of derisking and debanking. RBNZ would also have concerns if reporting entities were encouraged to take a 'judge and jury' approach and decline transactions where there were suspicions or actual evidence of money laundering, given the importance of due process. RBNZ also note that it could be impracticable and present potential health and safety risks, if frontline staff within reporting entities were encouraged to decline transactions to prevent money laundering.

Supporting the implementation of targeted financial sanctions

10. RBNZ supports an amendment to the AML/CFT Act or other relevant legislation that results in New Zealand meeting its international obligations, including targeting financial sanctions ('TFS'). It is RBNZ's view that the current regulations issued through the United Nations Act 1946 do not impose obligations for persons to take proactive steps to implement measures to prevent and detect financial services or property being made available to designated terrorists, e.g. it is simply an offence to provide financial services or property to a designated terrorist.
11. RBNZ considers the scope of TFS is broader than just reporting entities under the AML/CFT Act. This is mainly due to the wide definition of "property" under the United Nations regulations.
12. Through information obtained during on-site inspections, it is RBNZ's understanding that large reporting entities, who operate globally, have already implemented TFS policies, procedures, and controls.

Risk-based approach to regulation

Understanding our risks

13. RBNZ considers that s.58 of the AML/CFT Act needs redrafting to better highlight the pivotal nature of the risk assessment in reporting entity AML/CFT measures. For instance, the s.58 "must have regards to" wording needs more prescription to remove the vagueness. Another example is s.58(g) and the use of supervisory guidance which again needs more prescription and legal effect especially with instances of derisking. A practical application of this would be the mandated use of more nuanced supervisory risk assessment findings to stem derisking in the remittance sector. A good example of this is the Department of Internal Affairs New Zealand-to-Pacific risk assessment.
14. In addition, RBNZ submits that specifically s.57(1)(l) of the AML/CFT Act needs to be clearer and more prescriptive, particularly with reference to internal communications and training.

Balancing prescription with risk based obligations

15. Guidance will be essential in helping reporting entities meet any proposed 'minimum standards' of the AML/CFT Act. These standards will need to be proportionate and developed carefully in partnership with industry, and incorporate international standards. Having minimum standards will help sectors have a uniformity of professional conduct and will help protect consumers. An example of this would be the creation of competency based licencing regimes which would increase AML/CFT capability and set professional and AML/CFT standards which are properly audited and supervised.
16. The AML/CFT Act is activity based. This has proven to be a more elegant model than some other AML/CFT legislation around the world which defines business types. However, a review of the definitions of activities covered by the AML/CFT Act should be undertaken to ensure the current wording is fit for purpose. For instance, new activities could cover new forms of remittance, the use of mobile money operators, the application of new technologies, virtual asset service providers, and new financial instruments.

Mitigating unintended consequences

Financial inclusion or exclusion

17. The unintended consequences of the AML/CFT Act can lead to derisking, difficulties with maintaining correspondent banking relationships, onerous compliance burdens for low risk entities and overly expensive compliance programmes.
18. Financial inclusion, including stemming derisking, easier access to banking services, use of cash, remote onboarding and electronic know-your-customer facilities will need consideration as part of the statutory review. The AML/CFT Act review should consider revisiting identity verification requirements and processes to ensure they are still fit for purpose and are future proofed as best it can. This will include greater clarity around obtaining and verifying identity electronically, the current use and future of biometrics, the increasing prevalence of remote onboarding for those with reduced access to services and continued use of cash in an increasing cashless society.
19. In terms of the unintended consequences include derisking, lack of competition, correspondent banking relationship withdrawal, and financial exclusion. Work on this topic should mirror ongoing Financial Action Task Force ('FATF') projects on unintended consequences of AML/CFT standards and cross border payments. Consultation with the RBNZ and Ministry of Foreign Affairs and Trade will also be of benefit. Further input on this topic can be provided separately.

New Zealand's cash system and related digital innovations

20. The way AML/CFT regulations are being applied by reporting entities is giving rise to unintended spillovers affecting the efficiency, safety, and inclusiveness of New Zealand's cash system.
21. These spillovers could be reduced through further guidance on how the principles based regulations should be applied, as well as enhanced transparency and accountability arrangements for reporting entities and related digital innovations.

22. In some areas of the current AML/CFT regime it does not appear to be achieving the right balance between deterring and detecting ML/TF and addressing other important public policy objectives.
23. One example is the removal of fast cash deposit boxes from banks. These were commonly used by retailers to bank their excess cash. Some banks determined that fast deposit boxes made it difficult to determine where cash was obtained from and so presented a ML/TF risk. However, the impact of this decision is that retailers need to find alternative ways of depositing cash, which often means holding excess cash outside of the banking system or feeding bank notes into Smart ATMs and exposing themselves to personal safety risks by doing so.
24. RBNZ is aware of people that undertake legitimate work but which often involves cash payments (for reasons including privacy) finding it difficult to deposit that cash in banks due to their implementation of AML/CFT requirements. This can have an impact on financial inclusion and in more extreme cases may encourage behaviour such as underreporting of income or tax evasion.
25. RBNZ is aware that AML/CFT compliance is often cited as a reason for debanking both for individuals with difficult circumstances (such as difficulty obtaining identity information or cash use as mentioned above) and newer fintech companies that pose novel risks that banks find difficult to assess and manage. This has potential impacts for financial inclusion and for innovation and productivity growth.
26. The Money and Cash department is progressing various future focused workstreams, to steward a money and cash system in New Zealand that is fit for purpose, and for the future. This includes considering a potential central bank digital currency, monitoring digital innovations in private money and payments such as crypto assets, and redesigning a more efficient cash system.
27. As these workstreams develop, and as supporting regulatory mechanisms shape up, we would like to work with MOJ and Department of Internal Affairs ('DIA') to consider relevant AML/CFT requirements, and how AML/CFT obligations are placed throughout the system. This reflects that our various workstreams may alter the roles played by different parties in the system and give rise to new digital or cross border challenges.

Powers and functions of AML/CFT agencies

Supervising implementation of targeted financial sanctions

28. RBNZ supports the extension of its existing supervisory powers and functions under the AML/CFT Act to also include TFS. However, it is RBNZ's view that the scope of RBNZ supervised population should remain as registered banks, non-bank deposit takers, life insurers, and relevant designated business group members.

29. A number of existing AML/CFT systems and controls within reporting entities (particularly registered banks) are also used to comply with TFS obligations, e.g. politically exposed persons screening solutions. RBNZ is already familiar with a number of these TFS systems and controls. However, RBNZ acknowledges that additional specialist resources and skills would be required if RBNZ was to supervise its reporting entities for compliance with TFS obligations.
30. While RBNZ is comfortable to supervise its existing supervised population for TFS purposes, a broader question remains as to what agency or agencies would be responsible for other reporting entities and non-reporting entities, e.g. exporters.

Secondary legislation making powers

Codes of Practice

31. Codes of practice should be an operational decision with authority resting with the chief executives of the AML/CFT supervisors. This makes codes of practice more responsive to AML/CFT requirements; either for more timely and responsive law enforcement or industry purposes. An example of this is a code of practice created for subsectors such as low risk remitters and associated reliance and safe harbour function. This would be limited to a small part of the regime without the entire AML/CFT environment being changed as part of legislative or regulatory changes.

Licensing and registration

AML/CFT licensing for some reporting entities

32. Some sectors are currently unlicensed and could benefit from a competency based licencing regime. This would reduce ML/TF risk and increase AML/CFT capability and also provide greater transparency and consumer protection. It can also potentially reduce derisking in combination with high quality audits, successful supervisory interactions, and other supporting initiatives. However, costs associated with licencing regimes could be a barrier to effective operation and entry into some sectors.

Part 2. Scope of the AML/CFT Act

Challenges with existing terminology

Businesses providing multiple types of activities

33. RBNZ submits that the structure of the current AML/CFT Act could allow some activities or persons to 'slip between the cracks' and not be supervised. How something is captured by the AML/CFT Act is currently based on two main categories, firstly, the provision of certain financial activities and, secondly, whether you are a designated non-financial business or profession. However, New Zealand's supervisory framework is not based on the activities conducted by a reporting entity in the ordinary course of business. Instead, supervision is generally at an institutional or sector level, e.g. a registered bank. This could result in a person or business conducting a certain activity within a particular institution or sector that is not supervised by one of the three AML/CFT supervisors. In addition, this can also result in supervisory overlap, e.g. a registered bank offering real estate agent related services or a business not being captured.

Potential new activities

Non-life insurance businesses

34. It is RBNZ's view that non-life insurance businesses may very well hold valuable transactional data that could potentially help New Zealand agencies enrich financial intelligence. However, RBNZ believes this could be achieved only if these businesses are fully covered under the AML/CFT Act. RBNZ submits that full capture of all non-life insurers would be disproportionate to the ML/TF risks posed by these entities. There may be numerous issues and significant administrative difficulties in achieving the desired outcome, including a largely unsophisticated market, very many small players, and lack of staff knowledge. There would also be additional supervisory costs to supervisors as RBNZ's supervised population would double in size. The supervision of a single obligation seems disproportionate.
35. RBNZ considers that a cost-benefit analysis would need to be completed. An alternative option has been adopted by Ireland to find different ways of obtaining the type of transactional data sought by law enforcement, rather than regulatory change.

Currently exempt sectors or activities

How does the AML/CFT Act apply to RBNZ as an entity?

36. The Reserve Bank is currently excluded from the reporting requirements of the AML/CFT rules (defined by exclusion in Definitions regulations). These regulations were due to expire in July 2021 but have been amended and do not have a further expiry date.
37. This appears to be consistent with treatment internationally, with other central banks are generally excluded from much of the AML/CFT obligations on the basis that the Bank's financial services activities form part of its central banking policy functions and/or present low or no ML/TF risk.

38. RBNZ has internal processes in place around due diligence and ML/TF detection, and a cooperative relationship with the New Zealand Police. This includes to manage any ML/TF risks associated with the Money and Cash department's interactions with the public returning unfit or damaged currency to the Reserve Bank.
39. We consider the RBNZ's exemption remains fit for purpose. However, we are currently progressing work on a range of initiatives that may impact the nature and scale of the ML/TF risks that arise from the RBNZ's activities. This includes work on a central bank digital currency. We will work closely with the MOJ on this work to ensure that any central bank digital currency is designed in a way that appropriately addresses ML/TF risks.

Managing intermediaries exemption

40. RBNZ submits that there is strong correlation between the AML/CFT Act's 'beneficial owner' definition and the managing intermediaries exemption. It is RBNZ's view the 'beneficial owner' definition has been applied too broadly and does not align to the FATF definition. In practice, when dealing with intermediaries, reporting entities are essentially expected to 'Know their customer's customer'. RBNZ acknowledges that the managing intermediaries exemption was intended to partially reduce the compliance burden on reporting entities. However, the exemption is not necessary and should be revoked if the 'beneficial owner' definition is amended and applied correctly.

Part 3. Supervision, regulation, and enforcement

Agency supervision model

42. RBNZ is supportive of New Zealand's current AML/CFT supervisory framework, comprising of the three AML/CFT supervisors, RBNZ, Financial Markets Authority and the DIA. From a RBNZ perspective, there are strong synergies between RBNZ being both a prudential regulator and an AML/CFT regulator. Matters identified by RBNZ's prudential teams can also have some significance from an AML/CFT perspective, e.g. underinvestment in systems or governance weaknesses. Vice versa, matters identified by the AML/CFT supervision team can be relevant to the prudential teams, e.g. a poor AML/CFT culture could indicate wider risk management concerns.
43. The three AML/CFT supervisors work collaboratively and effectively on an ongoing basis and this was highlighted as part of New Zealand's Mutual Evaluation. The current supervisory framework allows specialist sector knowledge and expertise within existing agencies. Where there is crossover, one supervisor can call upon the skills and guidance of another supervisor to assist, e.g. assisting during an on-site inspection.
44. For the abovementioned reasons, RBNZ supports maintaining the existing supervisory framework and welcomes further consideration of ways to improve AML/CFT supervision practices.

Mechanisms for ensuring consistency and responsiveness

45. While RBNZ acknowledges that there can sometimes be actual or perceived inconsistencies between supervisors' interpretations, the three AML/CFT supervisors have implemented processes via the Sector Supervisors' Forum to address these concerns and to ensure consistent interpretations. RBNZ also acknowledges that the issuance of triple-branded guidance by the three AML/CFT supervisors is not always published and communicated in a timely fashion. In addition, sometimes a 'one size fit all' approach towards guidance is not the most effective approach. RBNZ submits that more tailored, sector specific guidance is needed and should allow each supervisor to be more responsive with their respective supervised sectors.

Powers and functions

Inspection powers – Approving the formation of a Designated Business Group

46. RBNZ submits that the AML/CFT Act should expressly require an AML/CFT supervisor to approve the establishment of a Designated Business Group ('DBG'). If an AML/CFT supervisor does not review and assess the eligibility criteria of a DBG application, and subsequently approve its formation, then there is a significant risk that the application is ineligible. RBNZ does not support a 'silence equates to approval' approach.

Regulating auditors, consultants, and agents

Independent auditors

47. RBNZ submits that there is a supply and demand issue when it comes to conducting AML/CFT audits and the quality of audits performed varies. It is RBNZ's view that some reporting entities consider the mandated s.59 audit to be a significant compliance cost and seek out the most cost-effective solution which can come at the expense of a robust auditing process to conduct their audit.
48. RBNZ leverages s.59 audits as they provide useful insights prior to conducting an on-site inspection. Audits can also provide excellent sources of information for desk based reviews. The quality of audits within RBNZ's supervised population are generally of a high standard, however, RBNZ is aware that this is not consistent across other sectors.

Consultants

49. RBNZ acknowledges that AML/CFT consultants may have a role to play in the AML/CFT ecosystem, e.g. assist with remediation activities. Engaging consultants is a choice for reporting entities to make as to whether and who to consult with, the obligation to comply remains with reporting entities. RBNZ considers that it is not the role of AML/CFT supervisors to promote or encourage the use of consultants as a way to meet the obligations of the AML/CFT Act. For this reason, RBNZ does not support the role of consultants being specified in the AML/CFT Act.

Offences and penalties

Comprehensiveness of penalty regime

50. RBNZ's AML/CFT supervision model is underpinned by a relationship model and outcomes focussed approach. However, there can be times where enforcement action is appropriate when material non-compliance is identified. It is therefore important that appropriate penalties are available to supervisors directly or through the court process.
51. RBNZ submits that the current AML/CFT penalty regime is inadequate. As identified during the FATF's 2020 Mutual Evaluation of New Zealand, the current sanctions and penalties available for non-compliance are not sufficiently proportionate or dissuasive, particularly for large registered banks. RBNZ submits, in theory, the maximum pecuniary penalty that could be sought against a reporting entity would be in the range of \$15-20 million. For large registered banks whose annual profits typically exceed \$1 billion, a pecuniary penalty of \$15-20 million is not a disincentive or dissuasive. RBNZ supports a comprehensive review and a substantial increase in the value of pecuniary penalties available under the AML/CFT Act.
52. RBNZ also supports extending AML/CFT supervisors' powers to impose administrative sanctions. RBNZ would welcome further discussion on this topic to define specific scenarios and applicable limits.

Sanctions for employees, directors, and senior management

53. RBNZ supports increased sanctions and personal liability (including pecuniary penalties) for employees, AML/CFT Compliance Officers, senior management, and directors. RBNZ submits that these sanctions should only be applied in extreme cases where there has been deliberate and/or systemic failures. RBNZ submits that increased personal liability is consistent with other international AML/CFT regimes.

Time limit for prosecuting AML/CFT offences

54. RBNZ submits that the limitation period for prosecuting an AML/CFT offence of three years after the offence was committed is too short. From RBNZ perspective, on-site inspections for some reporting entities can be five years apart (or longer). Based on the current three-year limitation period, there would be occasions when RBNZ would be unable to take any enforcement action where non-compliance was identified.

Part 4. Preventive measures

Customer due diligence

When CDD must be conducted

55. It is RBNZ's view that there are inconsistencies in the AML/CFT Act in terms of the circumstances of when it applies to existing customers and ongoing customer due diligence ('CDD') (ss 14 and 31).
56. It is RBNZ's view that it is unrealistic and an inefficient use of a reporting entity's resources to obtain verification information (to the same standard as new customers) for all pre-AML/CFT customers. Instead, a risk based approach should be adopted and verification information should only be reviewed if a material change occurs or a customer's ML/TF risk profile changes, e.g. a customer is subject to a suspicious activity report. RBNZ recommends further discussion with the private sector to develop an approach that balances ML/TF risks and an efficient use of resources.
57. RBNZ considers a comprehensive review of the Amended Identity Verification Code of Practice 2014 is required. This includes the types of identity documentation, trusted referee and, the certification process.

What information needs to be obtained and verified

58. RBNZ has received feedback from reporting entities that challenges the requirement to verify a person's address. RBNZ considers the removal of the requirement to verify a person's address would not impact New Zealand's level of compliance with the FATF Recommendations. RBNZ would support address information being obtained, but not verified. An alternative approach could be to only verify address in high risk scenarios, e.g. customer is a politically exposed person ('PEP').
59. RBNZ does not support the current requirement under s.22(1)(c) to obtain and verify source of wealth of a customer or funds for "complex or unusually large transactions". For large reporting entities, these types of transactions occur on a regular basis.
60. RBNZ questions whether enhanced CDD should be required to be conducted on all trusts. It is RBNZ's view that the ML/TF risks associated with trusts vary and there should not be a 'one size fits all' approach.
61. RBNZ submits that the "verification" wording for both simplified and standard CDD is not consistent. For standard CDD s.16(1)(a) states "take reasonable steps to satisfy itself that the information" is correct. This is contrasted by "satisfied it knows who the person is" with simplified CDD in s.20(1).
62. Source of wealth ('SoW') versus source of funds ('SoF') is an issue. RBNZ considers that the AML/CFT Act should be clearer on the circumstances where SoW is required versus where SoF is required. The AML/CFT Act currently appears to allow a reporting entity to 'pick and choose'. It is RBNZ's view that where enhanced CDD is triggered, SoW information should be the dominant requirement, compared to SoF. RBNZ considers SoF should be applied to more limited scenarios, e.g. an occasional transaction that is considered suspicious.

Politically exposed persons

Identifying whether a customer is a politically exposed person

63. RBNZ does not support a requirement for senior management to provide approval before a business relationship is established with a PEP. It is RBNZ's view that this requirement would be impractical and significantly impact the efficiency of New Zealand's financial system, i.e. new customers could not open and operate banks until several weeks later.
64. S.26 of the AML/CFT Act currently requires a reporting entity to take reasonable steps to determine whether a customer or beneficial owner is a customer. RBNZ supports extending the scope to also include 'persons acting on behalf of a customer' because these people can have the ability to move and transfer funds, and could also be a PEP.
65. RBNZ submits that the legislation should be explicitly updated to require ongoing measures to determine if existing customers or beneficial owners are a PEP. Currently, the legislation just focuses on when new business relationships are established.

Correspondent banking

66. RBNZ submits that s.29(2)(c) of the AML/CFT Act is problematic by inclusion of the word "effective". RBNZ interprets this section of the AML/CFT Act to require a correspondent to assess both the adequacy and effectiveness, i.e. how they operate in practice of a respondent's AML/CFT controls. RBNZ submits this is inconsistent with international approaches to correspondent banking relationships. Even the FATF guidance on correspondent banking states that correspondent banking relationships are built on 'mutual trust'. RBNZ submits the assessment should be limited to 'adequacy' of controls and not 'effectiveness'.

Money or value transfer service providers

Maintaining a list of agents

67. During consultation with remitters and banks, the need for clear visibility of remittance structure including use of agents was definite. The nature, size, and complexity of a customer (remitter) is a fundamental part of the risk assessment undertaken by banks. Remitters also need to understand the risks associated with their own corporate structure and have compliance measures to mitigate those risks. This includes monitoring and managing those agents such as vetting and training.

Wire transfers

Terminology involved in a wire transfer

68. Definitions around wire transfers need to be revisited to review if they are still fit for purpose. This includes the impact of new technologies and channels of delivery. For instance, the role of wire transfers in mobile money operator payments and how they impact on remittance. Credit card technologies are also evolving and consideration should be given to what extent these could practically be reported as a prescribed transaction.

Prescribed transaction reports

69. RBNZ submits that the current prescribed transaction reporting ('PTR') regime is not fit for purpose. At a high level, the current legislative requirements (including definitions) and the structure of how most international wire transfers are conducted do not align. This provides uncertainty for both AML/CFT supervisors and reporting entities. Further, the format of international payments is changing over the coming years via ISO20022.
70. For the purposes of this submission and due to the complexities of PTR, RBNZ does intend to provide detailed scenarios. However, the issues can be categorised into at minimum six main areas:
- a. Bulk and funding payments
 - b. The use of SWIFT MT 202 message types
 - c. Determining who has the obligation to report where multiple reporting entities or financial institutions are involved in the chain?
 - d. Wire transfer exclusions
 - e. The blend of international wire transfers and domestic wire transfers
 - f. Extending the reporting timeframe beyond 10 days.
71. RBNZ acknowledges that PTR can provide a rich source of financial intelligence. To help ensure quality reporting, there needs to be an alignment between the legislative requirements, the format of international payments and the Police FIU XML Schema. RBNZ welcomes further consultation on this complex topic and suggests the private sector be part of the consultation.

Reliance on third parties

Effectiveness of reliance provisions

72. RBNZ submits s.33(3A) of the AML/CFT Act should be revoked. This is a redundant section of the legislation, particularly s.33(3A)(c) which refers to an "approved class of entities". It is RBNZ's view that s.33(3A) is based on a dangerous assumption that an "approved entity" has conducted CDD to the required standard, where in fact it may not have. Some reporting entities will have long standing customers who were on boarded well before there were legislative obligations to verify a person's identity.

Designated business group reliance

73. RBNZ submits that the eligibility criteria within s.5 of the AML/CFT Act for being a member of designated business group ('DBG') is too prescriptive. It is RBNZ's view that the eligibility criteria should be more generic to allow a range of different legal entity types or arrangement to be a member of DBG.

Internal policies, procedures, and controls

Review and audit requirements

74. The AML/CFT Act currently requires a separate a review and an audit. It is RBNZ's view that this can result in considerable compliance costs, duplication, and inefficiencies. RBNZ also submits that consideration should be given to replacing the word 'audit' with 'independent review'. In addition, the Australian model also uses the terms 'independent review' which allows greater flexibility and could include an audit. New Zealand currently has a 'supply and demand' issue in terms of the number of reporting entities and the number of AML/CFT auditors.
75. Legislation should state that the purpose of independent audits is to test the effectiveness of a business's AML/CFT system. Effectiveness needs to be demonstrable. Not only to auditors but other reporting entities such as banks who require evidence of AML/CFT complaint customers before providing services. Proven effectiveness will help customers access and maintain banking services. This also applies to correspondent banking relationships and other areas where effectiveness of AML/CFT measures are important such as the Wolfsberg Questionnaire.
76. A code of practice (rather than guidance) setting out the steps that businesses should take when considering country risk could be useful. A reporting entity should have this already incorporated into their risk assessment which will have been informed by the National Risk Assessment and Sector Risk Assessment. However, guidance or even regulation can help formalise this, especially for lower capability entities such as small remitters.

Suspicious activity reporting

Improving the quality of reports received

77. RBNZ submits that there are practical challenges with the current reporting timeframe of three days after forming suspicion. For larger reporting entities, some suspicious activity reports originate from frontline staff who submit an 'unusual activity report' to the AML/CFT investigations team. The review and investigation can be several days later and could result in a suspicious activity report being submitted more than three days after the transaction was conducted. This is further compounded by the shift from a subjective test to an objective test for 'suspicion'¹. RBNZ encourages further consultation with the private sector on this matter.
78. RBNZ further submits that there is currently industry confusion regarding the reporting of fraud and scams via suspicious activity reporting ('SAR'). RBNZ considers fraud to be a predicate offence to ML and therefore actual or potential fraud identified by reporting entities should fall within the scope of SAR.
79. The AML/CFT Act does not currently permit sharing of SAR information with offshore parent companies. RBNZ submits that further consideration should be given to sharing SAR information for AML/CFT related purposes.

¹ Department of Internal Affairs v Ping An Finance (Group) New Zealand Company Limited [2017] NZHC 2363

Part 6. Minor changes

Definitions and terminology

80. RBNZ supports the proposed definition of a 'life insurer'.

SARs and PTRs

81. RBNZ supports the need to clarify and specify which agencies are responsible for supervising compliance with SAR obligations, especially on the quality and timing of their SARs.

Exemptions

82. RBNZ considers the current exemptions process does not give consideration to seeing exemptions through to their expiry date. There is currently no one agency responsible for assessing the compliance with the imposed conditions, both with adequacy and effectiveness.