NEW ZEALAND BANKERS ASSOCIATION

Submission

to the

Ministry of Justice

on the

Exposure Draft: Anti-Money Laundering and Countering Financing of Terrorism Amendment Bill

27 January 2017

NEW ZEALAND BANKERS ASSOCIATION
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About NZBA

1. NZBA works on behalf of the New Zealand banking industry in conjunction with its member banks. NZBA develops and promotes policy outcomes that contribute to a strong and stable banking system that benefits New Zealanders and the New Zealand economy.

2. The following fifteen registered banks in New Zealand are members of NZBA:
   - ANZ Bank New Zealand Limited
   - ASB Bank Limited
   - Bank of China (NZ) Limited
   - Bank of New Zealand
   - Bank of Tokyo-Mitsubishi, UFJ
   - Citibank, N.A.
   - The Co-operative Bank Limited
   - Heartland Bank Limited
   - The Hongkong and Shanghai Banking Corporation Limited
   - Industrial and Commercial Bank of China (New Zealand) Limited
   - JPMorgan Chase Bank, N.A.
   - Kiwibank Limited
   - Rabobank New Zealand Limited
   - SBS Bank
   - TSB Bank Limited
   - Westpac New Zealand Limited.

Background

3. NZBA welcomes the opportunity to provide feedback to the Ministry of Justice (**MoJ**) on the Exposure Draft: Anti-Money Laundering and Countering Financing of Terrorism Amendment Bill (**Draft Bill**), which implements of Phase Two of the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (**AML/CFT Act**), and commends the work that has gone into developing it.

4. If you would like to discuss any aspect of the submission further, please contact:

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Executive Summary

5. The following submission sets out NZBA's high-level feedback on matters in the Draft Bill. NZBA members will also provide their responses to the specific questions posed in the MoJ Information Paper in their own individual submissions.

6. NZBA supports the proposals to extend the AML/CFT Act's coverage to the businesses and professions outlined in the Draft Bill.

7. With regard to the suspicious activity reporting proposals, NZBA submits that:

   a. all reporting entities, including high-value dealers, should have the same obligations and therefore the proposed new section 40(5) should be removed; and

   b. there may be situations where a suspicious activity report may not be practical or feasible.

8. With regard to the changes aimed at reducing compliance costs:

   a. NZBA supports the expansion of the definition of a 'Designated Business Group' to include Phase Two reporting entities, however NZBA submits that it should also be expanded to include Limited Partnerships which are reporting entities.

   b. With regard to reliance on another business, NZBA has some reservations about the extent to which one reporting entity can rely on another reporting entity to conduct CDD, particularly in relation to the requirements set out in section 17 of the AML/CFT Act. NZBA also submits that placing reliance on another reporting entity's CDD should be conditional on the consent of the reporting entity being relied on.

   c. With regard to simplified due diligence, NZBA submits the proposal to extend simplified due diligence provisions to state-owned enterprises and subsidiaries of publicly listed entities in countries with sufficient AML/CFT systems does not go far enough and should also extend to regulated foreign financial institutions carrying on business in low risk overseas jurisdictions (as defined by FATF) and subsidiaries of New Zealand listed issuers.

   d. NZBA supports streamlining the ministerial exemptions process.

9. With regard to the other proposed changes to the legislation:

   a. NZBA submits that the information sharing proposals do not go far enough as they do not appear to allow information sharing between reporting entities in appropriate and defined circumstances.

   b. In light of there being no proposed change to the number of supervisors, NZBA supports the proposal that the Department of Internal Affairs (**DIA**) will be the AML/CFT supervisor for Phase Two reporting entities.

10. NZBA has a number of comments on the drafting of the Exposure Draft, including requests for clarification and comments on definitions.

Extension of the AML/CFT Act to cover additional businesses and professions

11. NZBA supports the inclusion of lawyers, accountants, real estate agents, conveyancers, high-value goods dealers and additional gambling service providers as reporting entities under the AML/CFT Act. In NZBA's view these businesses and

professions potentially present an inherently high risk of money laundering and accordingly NZBA submits that it is appropriate for them to be subject to the AML/CFT Act.

12. To ensure consistency of application, NZBA submits that all provisions of the AML/CFT Act be applied to the additional businesses and professions, subject to any clearly defined and regulated exceptions or exemptions which are justified and appropriate. NZBA submits that any exceptions or exemptions approved should be consistent with ensuring the AML/CFT Act's principles remain intact, and its objectives continue to be achieved.

13. Enhancing our AML/CFT regime in this respect in line with FATF Recommendations is an important part of building New Zealand's reputation as a jurisdiction with a strong commitment to combatting money laundering and terrorist financing.

Suspicious activity reporting

High-value dealers

14. Proposed new section 40(5) (clause 16) proposes that a high-value dealer "may" report a suspicious activity, or proposed activity, to the Commissioner. It is unclear why all other reporting entities "must" report suspicious activity (as per proposed new section 40(3)), while this will only be optional/discretionary for high-value dealers.

15. NZBA submits that there is actual evidence that high value assets (particularly motor vehicles and precious stones) have been used by criminals in the placement and layering phases of money laundering.[1] NZBA submits that dealers in such assets should not be provided an 'option' to report suspicious activity where there are reasonable grounds to suspect money laundering or terrorist financing.

16. NZBA submits that an 'optional' requirement for high-value dealers will create deficiencies in New Zealand's AML/CFT framework. In order to ensure that the Phase Two reforms are robust, all reporting entities, including high-value dealers should have the same obligations regarding suspicious activity reporting and therefore proposed new section 40(5) should be removed.

Potential issues

17. NZBA submits that, in many cases, suspicious activity may constitute an enquiry by a member of the public to avoid AML/CFT requirements. For example, a non-customer asking if a reporting entity requires identification for a certain activity or transaction(s), followed by the non-customer leaving/terminating the interaction without providing a name or any other identifying information.

18. Under the Draft Bill, in such circumstances a reporting entity would be required to report this to the Police Financial Intelligence Unit (**FIU**). A reporting entity would do

[1] http://www.police.govt.nz/sites/default/files/publications/fiu-quarterly-typology-report-q3-2014-2015.pdf

so by reporting the circumstances/activity involving an unknown person and, where possible, providing CCTV/telephone recording footage. Whilst this may be useful to indicate that an unknown person may be trying to avoid AML/CFT requirements, generally speaking, the FIU will not currently accept a report of this nature as it cannot be linked to a person/entity. Even in instances where the FIU would accept these types of reports, it would be extremely difficult to link any activity of this nature occurring across multiple reporting entities, possibly over a long period of time, between each instance.

19. Furthermore, even if the FIU were able to link the activity, they would still only have an unknown person possibly asking AML/CFT related questions. In the investigation priority matrix for law enforcement agencies, this type of activity would in all likelihood to be of a lower priority and not be actively investigated.

20. NZBA submits that situations such as this (where it is not feasible or practicable to make suspicious activity reports) should be exempted from the requirements and clear guidance should be issued by the AML/CFT Supervisors (in consultation with the FIU) outlining the proposed extent of this obligation.

Changes aimed at reducing compliance costs

General comment

21. NZBA members have thus far found it difficult to identify what could lead to less of a financial impost on reporting entities.

Definition of Designated Business Group

22. NZBA supports the expansion of the definition of a 'Designated Business Group' to include Phase Two reporting entities. However, NZBA submits that the definition should also be expanded to include Limited Partnerships which are reporting entities.

23. Under the Draft Bill, reporting entities which are Limited Partnerships would not be eligible to become members of a DBG. Consequently, Limited Partnerships would not be able to reap the relevant benefits and potentially reduced compliance costs.

Reliance on another business

The need for consent

24. NZBA has some reservations regarding the practicalities of relying on other reporting entities to conduct CDD. A key component of conducting CDD is understanding the nature and purpose of the proposed business relationship between a customer and reporting entity (in addition to collecting identification documents), and determining in any given situation whether enhanced CDD should be completed (section 17 of the AML/CFT Act). This helps to inform whether or not the activity that flows through the reporting entity is normal for that customer or is unusual/suspicious. Therefore the reporting entity being relied upon would need to make those "nature and purpose" enquiries on behalf of the party seeking to rely on them (which would only be

appropriate/relevant in a limited set of circumstances, such as a managed fund arrangement where the manager effectively administers everything on behalf of the reporting entity that has legal title to fund assets and is well placed to make those enquiries). Otherwise that aspect of CDD could not practically be outsourced and would still need to be done by the primary reporting entity. Using a registered bank as an example, a new reporting entity (such as an accounting firm) could not practically rely on the CDD performed by a bank on a mutual customer as the bank would not be in a position to comply with the requirement of section 17 of the AML/CFT Act in relation to the client/accounting firm relationship.

25. As previously raised in the NZBA submission on the Consultation Paper: Improving New Zealand's ability to tackle money laundering and terrorist financing (**Previous NZBA Submission**), NZBA has concerns about placing reliance on another reporting entity in the absence of any written agreement or consent.

26. NZBA submits that clause 13 should be amended to make reliance on another reporting entity's CDD conditional on the relying reporting entity obtaining the consent of the primary reporting entity prior to reliance taking place.

Existing Customer Due Diligence

27. NZBA supports the inclusion of a definition of an "existing customer" in clause 5(3) of the Draft Bill. NZBA submits however that guidance should be issued clarifying what the Supervisors' expectations are in relation to "existing customers", and when an "existing customer" is no longer considered as such (for example, when they begin a relationship with another reporting entity) to avoid misinterpretation and unintended non-compliance.

Simplified Due Diligence

28. NZBA submits that the proposal to extend simplified due diligence provisions to state-owned enterprises and subsidiaries of publicly listed entities in countries with sufficient AML/CFT systems does not go far enough.

29. As raised in the Previous NZBA Submission, NZBA supports extension of the provisions to regulated foreign financial institutions carrying on business in low risk overseas jurisdictions (as defined by FATF). Examples of these institutions are banks that are regulated for AML/CFT purposes in a low risk foreign jurisdiction but which are not publicly listed on an overseas exchange. There is typically a large amount of publicly available information that exists as to their management and ownership structures, and, from a money laundering perspective, these institutions are generally considered as having more effective policies, procedures and controls due to their regulated nature.

30. Further, the Consultation Paper: Improving New Zealand's ability to tackle money laundering and terrorist financing signalled that MoJ is looking to extend simplified due diligence provisions to subsidiaries of New Zealand listed issuers as well as overseas listed issuers, however the proposed new section 18(2)(o) appears to limit this to just subsidiaries of overseas listed issuers.

Streamlining the Ministerial exemptions process

31. NZBA supports streamlining the ministerial exemptions process. NZBA welcomes any measures taken to increase the efficiency of the process and reduce the time taken to obtain the required approvals.

32. NZBA submits that change is required to the existing process. Within our members' DBGs some reporting entities have incurred unnecessary costs due to deficiencies in the current process. 'Workarounds' or waivers from AML/CFT supervisors have had to be obtained due to the delays.

33. NZBA submits that the AML/CFT Act and supporting regulations are technical by nature and can potentially result in unintended consequences. Therefore it is imperative that there is an efficient ministerial exemption process to ensure that the correct entities and relevant activities are subject to the AML/CFT legislation.

Other changes to the legislation

Information sharing

34. NZBA submits that the information sharing proposals in clauses 32-34 of the Draft Bill do not go far enough as they do not appear to allow information sharing between reporting entities in appropriate and defined circumstances, although the MoJ Information Paper notes there may be information sharing among reporting entities "in limited cases".

35. As raised in the Previous NZBA Submission, NZBA submits that the AML/CFT regime would benefit significantly if reporting entities were able to share financial intelligence/customer information with other reporting entities (and indeed their own offshore counterparts) in appropriate and tightly defined circumstances. This would greatly enhance the ability of reporting entities to more accurately and effectively investigate suspicious activity where an activity or transaction that involves another reporting entity occurs.

36. In support of this submission, NZBA notes section 314(b) of the USA Patriot Act provides US financial institutions with the ability to share information with one another in order to better identify and report potential money laundering and terrorist activities. Financial institutions must establish and maintain procedures to safeguard the security and confidentiality of shared information, and must only use shared information for strictly limited purposes.[2]

Supervision

37. As noted in the Previous NZBA Submission, NZBA submits the model of supervision that would deliver the best outcomes for New Zealand is the single supervisor model. However, given MoJ's decision not to adopt this model, NZBA supports clause 31 of

[2] A useful factsheet relating to section 314(b) can be found at the following link: https://www.fincen.gov/statutes_regs/patriot/pdf/314bfactsheet.pdf

the Draft Bill that proposes the DIA will be the AML/CFT supervisor for Phase Two reporting entities.

38. NZBA submits that the proposed approach will increase the likelihood of consistent supervision by limiting the number of AML//CFT supervisors. Furthermore, there is existing AML/CFT supervision experience within the DIA.

39. NZBA submits that industry professional bodies are not appropriate to take on supervisory roles due to inherent conflicts of interest, as well as material lack of experience in an AML/CFT regulatory environment. NZBA prefers visible independence and transparency. Such a model would further contribute to the risk of inconsistent standards across industry sectors, reduce supervisor responsiveness to an ever changing AML/CFT environment, delay consultation processes and updates of regulatory guidelines, and promote the inefficient use of resources.

Drafting comments

Request for clarification

40. Clause 7 of the Draft Bill amends section 14 of the AML/CFT Act. NZBA submits that the drafting of these amendments should be clarified.

41. As amended, section 14 would read:

> ***14 Circumstances when standard customer due diligence applies***
>
> *A reporting entity must conduct standard customer due diligence in the following circumstances:*
>
> *(a) if the reporting entity establishes a business relationship with a new customer:*
>
> *(b) if a customer seeks to conduct an occasional transaction through the reporting entity:*
>
> *(c) if, in relation to an existing customer, and according to the level of risk involved,—*
>
> *(i) there has been a material change in the nature or purpose of the business relationship; and*
>
> *(ii) the reporting entity considers that it has insufficient information about the customer:*
>
> *~~(d) any other circumstances specified in regulations.~~*
>
> *(d) any other circumstances specified in subsection (2) or in regulations.*
>
> *(2) For the purposes of subsection 1(d), as soon as practicable after a reporting entity becomes aware that an existing account is anonymous, a circumstance occurs which the reporting entity must conduct standard customer due diligence in respect of that account.*

42. NZBA queries the drafting of this provision. Is subsection (2) meant to refer to (1)(d) or should the reference be to (1)(c)?

43. With regard to the proposed new section 49A (clause 17), and the new requirement to keep copies of suspicious activity reports for a period of longer than 5 years if so specified by the AML/CFT Supervisor or Commissioner, NZBA requests that reporting entities be given sufficient notification from the AML/CFT Supervisor or Commissioner to ensure that they are able to comply with this request the (i.e. the records will not be wiped after 5 years).

Definitions

44. Proposed new section 18(2)(o) refers to a "company". NZBA submits the reference should rather be to any publicly listed entity, as there could be issuers (for example, Limited Partnerships) that are not companies. Should this submission not be accepted, NZBA submits the definition of a company in this section be the definition of a company in section 2(1) of the Companies Act 1993, and also include an overseas company (also defined in section 2(1) of the Companies Act).

45. With regard to the reliance provisions, specifically the changes to section 33 (clause 13), NZBA queries whether 'approved entity' and 'approved class of entities' will be defined in Regulations and, if so, when are these Regulations expected to be issued. NZBA submits that clarification of these two definitions is imperative.

Amendments that have made the AML/CFT Act's requirements more conservative

46. NZBA has noted that in a few places the amendments have made the AML/CFT Act's requirements more conservative.

    a. Clause 5(5) amends the definition of "*occasional transaction*" in section 5 of the AML/CFT Act to capture cash transactions **equal to** and over the applicable threshold value (as opposed to just over).

    b. Similarly, clause 5(6) amends the definition of "*prescribed transaction*" to capture wire transfers and cash transactions of a value **equal to** or greater than the applicable threshold value.

    c. We also note that clause 13(1) amends section 33(2)(c)(ii) to change the timeframe for providing relevant verification information from "*not later than 5 working days*" to "*on request by the reporting entity but within 5 working days of the request*".

47. NZBA would welcome the amendment of the applicable thresholds for both occasional transactions and cash transactions to be the same amount of $10,000 – as currently they are currently proposed to be $9,999 and $10,000 respectively. This will assist in the systemisation of searches for relevant reportable transactions.