New Zealand Banking Association
Te Rangapū Pēke

Submission

to the

Ministry of Justice

on the

AML/CFT ‘Early’ Regulatory Package Exposure Draft

14 April 2023

NEW ZEALAND BANKING ASSOCIATION – TE RANGAPŪ PĒKE
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About NZBA

1. The New Zealand Banking Association – Te Rangapū Pēke (**NZBA**) is the voice of the banking industry. We work with our member banks on non-competitive issues to tell the industry's story and develop and promote policy outcomes that deliver for New Zealanders.

2. The following eighteen registered banks in New Zealand are members of NZBA:
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   - ASB Bank Limited
   - Bank of China (NZ) Limited
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   - China Construction Bank
   - 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
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   - KB Kookmin Bank Auckland Branch
   - Kiwibank Limited
   - MUFG Bank Ltd
   - Rabobank New Zealand Limited
   - SBS Bank
   - TSB Bank Limited
   - Westpac New Zealand Limited

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3. If you would like to discuss any aspect of this submission, please contact:

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Introduction

NZBA welcomes the opportunity to provide feedback to the Ministry of Justice (**MoJ**) on the AML/CFT 'Early' Regulatory Package: Exposure Draft (**Exposure Draft**). NZBA commends the work that has gone into developing the Exposure Draft. Our specific comments are set out in the table contained in the appendix to this submission. We have not commented on all proposals.

Two of the proposed amendments have the potential to reduce compliance costs, significantly streamline the AML/CFT process and add value to customers, but we do not consider that the current drafting achieves the potential benefits. These are:

- Address verification: we support the removal of address verification, but understand the current proposal as still requiring a reporting entity to check and validate the address as genuine. This proposal reduces intelligence value without reducing the compliance burden. We do not support the proposal in its current form, and would like to see the requirement be limited to address collection only.
- Prescribed Transaction Report (PTR) timeframe extension: the extension from 10 days to 20 days will only take place when a technology issue with an automated solution has occurred. We consider that this extension should apply more broadly.

We do not support the following amendments, as we consider they are impractical and/or will result in a negative impact on customers and staff that is disproportionate to any benefits that will occur. Furthermore, there are some that are too limited in their application. Further details are contained in the table, but briefly, these include:

- Potential additional enhanced customer due diligence measures – in particular, senior manager (i.e. direct report of the CEO) approval for certain transactions and business relationships.
- The limitations around the references to the Financial Action Task Force (**FATF**) Call to Action list and how this translates to jurisdictions considered high risk.
- We do not support the prohibition on establishing or maintaining correspondent relationships with **only** the Democratic People's Republic of Korea, this is too narrow.
- Inability to apply Simplified Customer Due Diligence (**SCDD**) where a suspicious activity report (**SAR**) is raised (most likely to impact ongoing customer due diligence, as SCDD is generally carried out up-front, with a SAR likely to arise later in the course of a business relationship).
- Identification and verification of settlors of trusts.
- Customer due diligence for low value payments outside of a business relationship or occasional transaction (e.g. third party depositors).

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Reference	Proposal	NZBA Response
	Part 1 – addressing areas of risk	
High Risk Countries Stat review rec 187 AML/CFT (Requirements and Compliance) Regulations: 38(15)	Prohibit businesses from establishing or maintaining correspondent relationships with Democratic People's Republic of Korea banks, in line with the Call for Action issued by the Financial Action Task Force.	In principle we support the prohibition of correspondent relationships with high-risk nations, but we do not support the specific reference to only the Democratic People's Republic of Korea. There are other countries on FATF's Call for Action list, and further countries could be added at any time. The regime should be flexible enough that other countries can be added without a lengthy process.
High Risk Customers: Legal Persons and Arrangements Stat review rec 121 and 116 AML/CFT (Requirements and Compliance) Regulations: 34	Prescribe that reporting entities must obtain, as part of customer due diligence (**CDD**), information about legal form and proof of existence, ownership and control structure, and powers that bind and regulate, and verify this information according to the level of risk. Require reporting entities to obtain the identity of the settlor or protector of a trust, nominees in relation legal persons, and other equivalent positions for other types of legal arrangements to ensure reporting entities are taking reasonable steps to verify the beneficial ownership of these customers.	In relation to the first proposal, we do not support this requirement without considerable further explanation as to the rationale and exact requirements. Our specific questions/comments include: • It is unclear what is meant by "powers that bind and regulate", and we consider that it would place a burden on bank staff beyond what can reasonably be expected – they should not have to review, interpret and understand significant legal requirements outside of the AML/CFT regime. • As identification and verification (**ID&V**) of entities is already a requirement along with ID&V of beneficial ownership and control structure, it is unclear what would additionally be required. In relation to the second proposal, we recommend this regulation be removed and further guidance be issued instead. We aren't clear why this requirement has been added; there is already a requirement to verify all those with effective control. There are a range of scenarios where it

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		will be very complicated or not possible to complete CDD on a settlor, for example, if the settlor is deceased or no longer has contact with the trustees. Additionally, if the settlor is a professional lawyer or accountant, we do not see a benefit from doing CDD on them. Additional burden could be placed on reporting entities trying to prove that they don't need to verify the settlor. We consider the current beneficial owner definition, which requires reporting entities to identify and verify effective controllers, is sufficient. If MoJ feels this definition is not sufficient, we consider that it is more appropriate to update the CDD Trust Factsheet and/or Beneficial Ownership Guideline and/or EDD Guideline. If MoJ feels that this requirement should remain, we would welcome regulatory relief for circumstances where it is not possible to conduct CDD on the settlor or protector.
Suspicious Activity Reports and Customer Due Diligence Stat review rec 127 and M6.1.9 AML/CFT (Requirements and Compliance) Regulations: 37	Prescribe that CDD must be conducted if a person seeks to conduct an activity or transaction through a reporting entity that is (a) outside a business relationship, (b) not an occasional transaction or activity, and (c) where there may be grounds to report a suspicious activity as per section 39A of the Act. Declare that simplified CDD is not appropriate where there may be grounds to report a suspicious activity as per section 39A of the AML/CFT Act.	We expect that this requirement will be challenging. Mandating that CDD must be completed if a transaction is suspicious will raise certain risks, including staff safety, as some people may get aggressive if declined. Additionally, there may be workability issues with the proposal for some banks, who wouldn't know until post-transaction that there were grounds to report a suspicious activity. These banks would need to effectively lower their third party deposit threshold to $0 and capture everyone (irrespective of channel – e.g. over the counter or smart ATMs). If this requirement is introduced, it may also lead to

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		third party transactions becoming prohibited, impacting customers. There is a problem with the drafting here in that it talks about 'if a **customer** seeks to conduct…' however, if the transaction is not an occasional transaction, 32(1)(a) and there is no business relationship, 32(1) ("outside of a business relationship"), then they cannot be considered a customer (refer to the definition of a customer in s5 of the AML/CFT Act). The 'customer' is not a facility holder or conducting an occasional transaction. If this requirement goes ahead, we recommend including a clear scope of what constitutes an activity or transaction outside a business relationship.
High Risk Customers: Additional Enhanced CDD Measures Stat review rec 124 AML/CFT (Requirements and Compliance) Regulations: 37	Prescribe that reporting entities must implement any additional enhanced customer due diligence measures at the start and for the duration of a business relationship as are required to mitigate the risks and provide a list of potential additional measures the reporting entity may apply.	We do not support this requirement as it is currently drafted, as we consider that the current proposal will likely increase the compliance burden without necessarily mitigating the risks. It is also very prescriptive and therefore going against the risk based approach. A reporting entity is already obliged to assess the risks posed by customers and the transactions/business dealings to be undertaken by those customers, etc and to put in place appropriate controls to satisfactorily mitigate against such identified risks. Those risks are required to be set out in a risk assessment, and supported by a compliance programme. We query whether these proposed new obligations are warranted – as we expect that reporting entities will already be addressing

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		such elevated customer risks through existing risk assessments and compliance programmes. In saying that, we are supportive of further clarification being provided, through guidance, on additional measures that can be taken but discretion should be left to the reporting entity as to which measures they use.
Part 6 – Clarifying obligations		
Customer Due Diligence Stat review rec 139 AML/CFT (Definition) Regulations: 8	Prescribe appropriate customer due diligence obligations for the formation of a legal person or legal arrangement. This should include a requirement to identify and verify the identities of the beneficial owners of the (to be formed) legal person or arrangement, as well as any person acting on their behalf.	Can more clarity be provided on the meaning of 'Prescription'? Is this to expand the scope of customer definition and perform CDD on them?
Customer Due Diligence Stat review rec 185 AML/CFT (Requirements and Compliance) Regulations: 38	Prescribe that the references to countries with insufficient AML/CFT systems or measures in place in sections 22(1)(a)(ii), 22(1)(b)(ii), and 57(1)(h) refer exclusively to those countries identified by the AML/CFT (Requirements and Compliance) Regulations: 38 19 Financial Action Task Force as being high risk jurisdictions subject to a Call to Action.	We do not support this proposal as we consider the drafting is too limited. The FATF Call for Action list is one of a number of sources our members use to determine high risk countries, and narrowing the definition to just this list is far too restrictive.
Record keeping Stat review rec M6.2.2 AML/CFT (Requirements and Compliance) Regulations: 38	Require reporting entities to keep records of prescribed transaction reports, account files, business correspondence, and written findings for five years.	This is a very broad requirement – we would welcome clarity on triggering criteria and specific details/information on account files, business correspondence and written findings to be retained.

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Customer Due Diligence: beneficial owner Stat review rec 118 AML/CFT (Definitions) Regulations: 7	Clarify that the definition of beneficial owner includes a person with ultimate ownership or control, and only applies to a "person on whose behalf a transaction is conducted" that meets this threshold, whether directly or indirectly.	We are supportive of this requirement however it does introduce new language that is not otherwise defined in the AML/CFT Act e.g. 'ultimate ownership', but would welcome clarity on: • The meaning of "ultimate ownership or control" of the customer, and how this differs from effective control. • The definition of "person on whose behalf a transaction is conducted". Providing examples of these individuals and the associated risks would be helpful. • The requirements for identification, the extent of independent verification required and the ability or circumstances to seek client confirmation for both intermediary owners and ultimate beneficial owners.
Customer Due Diligence: Risk Based Stat review rec 133 AML/CFT (Requirements and Compliance) Regulations: 37	Explicitly require that reporting entities risk rate new customers as well as require reporting entities to consider and update risk ratings as part of ongoing customer due diligence and account monitoring over the course of a business relationship.	We support this requirement but the wording should be broad enough to not require the risk rating to necessarily be recorded in each customer's record on a system or file, but allow for a rules-based approach (e.g. outlining the criteria / rules for when a customer is a certain risk rating), so as to provide flexibility and minimise the potential associated costs of systems and process changes. We also note that it will be significant to implement, and sufficient time will be required, particularly if systems changes will be necessitated to record risk ratings in each customer's records.
Customer Due Diligence: Risk Based Stat review rec 135	Require reporting entities to, according to the level of risk involved and as part of ongoing customer due diligence (**OCDD**), update (for a post-Act customer) or obtain (for an existing customer) customer due diligence information if required.	It is unclear whether the intention of regulation 12E is to create a higher standard of OCDD where a reporting entity's customer is a designated non-financial business or profession.

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AML/CFT (Requirements and Compliance) Regulations: 38		It is still not clear that, where it is necessary to update or obtain CDD information, should this be to the standard of the AML/CFT Act? Is this requirement leading us to uplift all existing customers to the current standards?
Ongoing CDD: information for account monitoring Stat review rec 134 AML/CFT (Definitions) Regulations: 37	Clarify that the requirement of section 31(4)(a) and (b) to review a customer's account activity, transaction behaviour and customer due diligence information (or for an existing customer, other information held) is according to the level of risk involved.	The expectations should be clearly identified as to what constitutes a risk based approach that differentiates customer due diligence vs account activity vs transaction behaviour.
Part 7 – Improving transparency of payments		
Stat review rec 169 AML/CFT (Requirements and Compliance) Regulations: 38	Require ordering institutions to obtain and transmit name and account or transaction numbers for an originator and beneficiary of an international wire transfer below NZD 1,000 and specify that this information does not need to be verified unless there may be grounds to report a suspicious activity report.	We are supportive of this recommendation in principle, but further consideration is required as this will be a significant piece of work.
Stat review rec 174 AML/CFT (Requirements and Compliance) Regulations: 38	Require beneficiary institutions to specify in their compliance programme the reasonable steps they will take to identify international wire transfers lacking required originator and beneficiary information. These measures should be risk-based and can include post-event or real time monitoring where feasible and appropriate	As above, we are supportive of this recommendation in principle, but further consideration is required as this will be a significant piece of work.
Stat review rec 197	Prescribe or exempt specific transactions (e.g., MT202s and certain currency exchange	We note that there is no corresponding regulation within the draft consultation pack which addresses the topics of MT202

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AML/CFT (Prescribed Transaction Reporting) Regulations: 40 (9)	transactions) from requiring prescribed transaction reporting, including requiring reports when a remittance provider deposits cash into a beneficiary's bank account to settle an inbound remittance.	message types or certain foreign currency transactions. In principle, NZBA supports exemptions being issued in these areas. We have no comment in relation to the other items noted, related to remittance provider transactions.
Part 8 – Providing Regulatory Relief		
Address verification Stat review rec 114 AML/CFT (Exemptions) Regulations: 31	Exempt all reporting entities from conducting address verification for all customers, beneficial owners and persons acting on behalf of a customer other than when enhanced CDD is required and instead require businesses to verify, according to the level of risk, that an address as genuine.	We do not support this proposal in its current form. Our strong preference is that reporting entities only be required to collect address information, without any obligation to verify that the address is genuine. One of the key stated objectives of MoJ, when undertaking the statutory review, was to reduce areas of unnecessary compliance burden, cost and complexity for reporting entities where possible. Removal of address verification was touted as the lowest of the low hanging fruit, which was costing industry a disproportionate amount of compliance resource/cost relative to the low value of performing the activity. The draft regulation proposes to replace the existing address verification requirement with a new requirement that businesses must verify, according to the level of risk, that an address is genuine. This requirement will still place a compliance burden on banks, without a corresponding practical benefit. Relief in this area would ideally be introduced earlier than 1 June 2024, if possible

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Other Stat review rec 115 AML/CFT (Requirements and Compliance) Regulations: 37	Declare that reporting entities can use reliable (but not independent) verification data, documents, or information in circumstances where a reliable and independent source of information does not exist. This does not apply to biographical information or information regarding source of wealth or source of funds.	It is unclear whether the application of this provision is limited to address verification only (and possibly to "nature and purpose" enquiries). If it is intended to be read narrowly, existing exemption handling procedures are likely to be sufficient in our view. This would be difficult to operationalise for a large reporting entity in particular, as staff would need to determine when a document "does not exist" as opposed to when the customer simply does not have the document. If this refers only to address verification (and possibly "nature and purpose" enquiries), its usefulness is limited. Should this provision also be intended to be applied more broadly, as inferred by reference to biographical information and source of wealth/funds, we consider that the proposal should not explicitly exclude source of wealth from being an acceptable 'reliable but not independent' source of verification data. In some cases there may be utility in substantiating source of wealth using reliable but not independent information in absence of anything else practicably available. For example the source of wealth for a trust that has been a customer of the Reporting Entity for many years, or is longstanding (e.g. 50 years old) might be best substantiated from the entity's own records (i.e. not independent) as the best SOW information practicably available.
Other Stat review rec 126	Prescribe the process that reporting entities must follow when conducting enhanced customer due diligence (**ECDD**) on trusts,	We are supportive of reducing the burden/ removing the requirement to complete ECDD for *all* trusts, however, we consider the legislation should remain high level and risk

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AML/CFT (Requirements and Compliance) Regulations: 37	including identifying types of trusts that are suitably low risk and other factors to consider when assessing the level of risk. Where trusts are suitably low-risk, exempt reporting entities from the requirement to obtain and verify relevant information about the source of wealth or source of funds.	based, with reporting entities able to determine in their own Programmes, and according to their own risk assessment, the scenarios where ECDD is not required. If the Regulations are too prescriptive, it is difficult to change and does not allow for a risk-based approach. Alternatively, guidance could be produced to provide the level of detail that reporting entities might want/need to help them determine the scenarios where ECDD is not required.
Other Stat review rec 132 AML/CFT (Requirements and Compliance) Regulations: 37	Enable a senior manager of a customer (that has been identified and verified in accordance with sections 19-20) to delegate authority to employees to act on behalf of the customer by electronic means with appropriate conditions and requirements to manage any residual risks.	It is unclear how this would impact CDD requirements, for example, would the individual to whom the authority is delegated still need to meet ID&V requirements? We would welcome clarity as to what evidence is required to substantiate the delegation. We would also welcome clarity on the definition of acting on behalf of the customer by electronic means. Finally, if this is in relation to persons acting on behalf of a customer, and the customer qualifies for simplified customer due diligence (**SCDD**), why not just remove the requirement to identify and verify persons acting on behalf of the customer where SCDD applies? As it stands, the SCDD requirements are not truly "simplified" due to the requirement to verify the person acting on behalf of.
Other Stat review rec 205	Extend the timeframe for submitting PTRs from 10 to 20 days.	NZBA supports the general extension of the reporting timeframe from 10 working days to 20 working days. However, the current drafting does not achieve this objective. The drafting limits the application to situations

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AML/CFT (Requirements and Compliance) Regulations: 38 (new regulation 35)		where a reporting entity encounters issues with its automated reporting system which prevents it from achieving a 10 working day timeframe, and extends that timeframe to no more than 20 working days. This conditional drafting is at odds with the consultation document (which refers to no such conditionality) and requires further amendment to achieve the desired purpose. The regulation should be redrafted with the condition removed. For example: *This regulation applies to a reporting entity who conducts a prescribed transaction on behalf of a person but is unable to comply with the requirement to report the transaction to the Commissioner within 10 workings days of the transaction.*