FINANCIAL SERVICES FEDERATION

27 January 2017

The AML/CFT Consultation Team,
Ministry of Justice,
SX 10088
Wellington **By email**: aml@justice.govt.nz

Dear Team members,

Information Paper on Phase 2 of the AML/CFT Reforms

The Financial Services Federation ("FSF") wishes to comment on the above Information Paper dated December 2016 (the "Information Paper").

By way of background, the FSF is the industry body representing responsible and ethical finance and leasing providers in New Zealand. The FSF has over fifty members and affiliates providing first-class financing, leasing, and credit-related insurance products and services to over 1 million New Zealand consumers and businesses. The FSF's affiliate members include internationally recognised legal and consulting partners. A list of the current membership is attached to this submission as Appendix "A".

Most of the FSF's members are directly affected by New Zealand's AML/ CFT laws, and in particular most members are "financial institutions" for the purposes of the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 ("AML/CFT Act"). As such, they have an interest in the effective and efficient operation of the AML/CFT Act in all relevant sectors of the economy, as was reflected in the FSF's submission on the Ministry's earlier Consultation Paper of August 2016, and as further reflected in what follows.

In making this submission, the FSF does not intend to address each of the questions posed in the Information Paper, many of which are not directly relevant to FSF members. Instead the comments that follow will address only those parts of the Information Paper that are likely to affect FSF members or on which the FSF otherwise wishes to comment. Where possible, the headings used below are intended to correspond to the headings used in the Information Paper.

Phase 2 Businesses and Professions: In its submission on the Ministry's August 2016 Consultation Paper, the FSF expressed its support for the "Phase 2" extension of the AML/CFT regime to the relevant businesses and professions, which it considers to be an appropriate progression which has been well-signalled. Phase 2 continues to be supported by the FSF, and the FSF expects that it is not necessary to repeat its earlier comments in full in this letter.

Besides saying that what is now proposed in the current Information Paper (and in the draft Bill that accompanied it) seems to the FSF generally to be appropriate to extend the AML/CFT regime to the relevant businesses and professions, the FSF wishes to comment on three specific aspects of the Phase 2 proposals, as set out under the following 3 headings.

<u>Lawyers and accountants</u>: The “designated non-financial businesses or professions” to which Phase 2 will extend the AML/CFT regime include lawyers and accountants, and the activities in respect of which the proposals would require lawyers and accountants to undertake customer due diligence (“CDD”) would include –

> “*engaging in or giving instructions in relation to transactions for customers related to creating, operating, and managing companies*”
>
> [That text is used on pages 2 and 5 of the Information Paper, and also in para (a)(vii) of the draft Bill’s definition of “designated non-financial businesses or profession”]

While it is not directly a concern of FSF members apart from those that are lawyers or accountants, that wording does seem to be very wide. Indeed, if “instructions” is read as including what is often described as “advice’’, then it may to have the potential to catch most advisory services provided by lawyers or accountants. The FSF doubts that is in fact necessary for AML/CFT purposes.

While it expects that this point may more appropriately be taken up by other industry bodies such as the New Zealand Law Society or Chartered Accountants Australia & New Zealand, the FSF notes that it would see merit in revised drafting which made clear that normal advisory services provided by lawyers or accountants that were not connected to specific payment transactions are not intended to be activities regulated by the AML/CFT Act.

<u>Businesses trading in “high value goods” - motor vehicle dealers in particular</u>: In its submission on Ministry’s August 2016 Consultation Paper, the FSF did not support the concept of dealers in high value goods having to comply with the full obligations currently applying to financial reporting entities under the AML/CFT Act as a result of Phase 2. Rather the FSF suggested a simplified regime for these businesses that would require them to report suspicious transactions.

The FSF notes that the Information Paper proposes that “high-value dealers” will only be required to undertake CDD in respect of goods sold for cash of $15,000 or more. The FSF fully supports this proposal on the basis that:

a) In part, the FSF’s earlier reservations about motor vehicle dealers being subject to the full range of obligations under the AML/CFT Act reflected a desire to avoid duplication in respect of vehicle finance, with both the financier and the dealer being required to undertake CDD in respect of the same vehicle sale. Under what is now proposed, such duplication is materially less likely, which is pleasing;

b) The FSF doubts if many vehicle sales involve cash in excess of $15,000 in any event;

c) The FSF notes that at page 10 of the Information Paper it is stated that –

    > “*If you decide you won’t accept cash above this amount, you won’t have any AML/CFT obligations. You could still accept electronic transactions of any amount*.”

    The FSF suspects that many motor vehicle dealers may adopt exactly that policy, and be outside the scope of the AML/CFT Act as a result;

<u>Businesses trading in “high value goods” - definition</u>: As noted above the intention is that that “high-value dealers” will only be required to undertake CDD in respect of goods sold for cash of $15,000 or

more. The draft Bill seeks to achieve that by defining "high-value dealer" in a manner that refers to sales where –

> "..*the total value of that transaction or those transactions are equal to or above the applicable threshold value [of $15,*000*]*"

The FSF suggests that is potentially ambiguous in that "total value" might be misread as referring to the aggregate amount of a dealer's sales, rather than to a specific sale. It suggests that a paragraph is added to the definition similar to the existing paras (c) and (d) of the definition but stating clearly that a person is not a "high-value dealer" in respect of any transaction which involves a sale price less than $15,000.

Proposed changes that affect compliance costs: The FSF wishes to comment on the following three proposals that are amongst those addressed under this heading in the Information Paper:

Proposals to require suspicious activity reporting: In its submission on the Ministry's August 2016 Consultation Paper, the FSF expressed doubts about the extension of suspicious transaction reporting to include reporting of "suspicious activity". In large part that was because such a change seemed likely to involve its members incurring further costs adapting the transaction reporting systems they already have in place, which in some cases include expensive transaction monitoring software. That expectation seems to be borne out by the fact that the Information Paper now addresses this proposal under a heading which assumes that the change will indeed "affect compliance costs".

Despite that, and while the FSF still expects that its members will incur costs due to the proposed wider focus of the reporting requirement, the FSF is pleased to see that while it is wider, the new definition of "suspicious activity" proposed by clause 16 of the draft Bill (that is, in proposed new section 39A remains very similar in scope to the existing section 40 of the AML/CFT Act.

While that is pleasing in some senses, the FSF still questions if this change is necessary. In particular –

a) In so far as support for this change has been based on FATF recommendations, the FSF repeats the point it made in its submission on Ministry's August 2016 Consultation Paper, namely that the FATF Recommendations actually require suspicious *transaction* reporting, and not reporting of "suspicious activity";

b) existing section 40(1)(a) of the AML/CFT Act already requires reporting where "a person conducts or seeks to conduct a transaction through a reporting entity" (language which is repeated in proposed new section 39A), and that may already catch suspicious activity even if it does not ripen into a "transaction": this too suggests the need for this change is not great;

For those reasons while the FSF accepts that the change in statutory language proposed here is in fact not major, it continues to doubt whether this change is in fact necessary.

Simplified due diligence: The FSF supports the Information Paper's proposal to allow simplified CDD in respect of SOEs and subsidiaries of listed companies, and also supports the proposal to relocate the description of other entities in respect of which simplified CDD is already permissible from regulations into the Act, as clause 8 of the draft Bill will do.

Streamlining the Ministerial Exemptions process: The FSF notes that clause 45 of the draft Bill will relocate what is presently a Ministerial power to grant exemptions with the Chief Executive of the

Ministry. That is likely to add efficiency to, and remove some cost from, the exemptions process and is accordingly supported by the FSF.

Other changes to the legislation:

Information sharing: In its submission on the Ministry's August 2016 Consultation Paper, the FSF expressed reservations about the then proposals for information sharing involving AML/CFT supervisors, Police and Customs. In that regard the FSF notes that clause 32 of the draft Bill proposes to replace the existing section 139 of the AML/CFT Act with a new provision that would allow information sharing only for the purposes of effective administration of the AML/CFT regime. The FSF now sees that as an improvement on the existing section 139, which is not qualified in that way.

Supervision: The FSF notes that the Information Paper proposes no change to the current supervisory arrangements, and agrees that none is needed.

Bringing existing regulations into the Act: The FSF also notes that the Information Paper proposes to move some provisions presently contained in regulations into the AML/CFT Act itself, including the information about beneficiaries that must be obtained when undertaking CDD on a trust. That provision is often applied by FSF members, and is sufficiently important to justify its relocation in the Act without change, which the FSF accordingly supports.

Supporting implementation:

Operational improvements to make the current requirements work better and reduce unnecessary compliance: Currently organisations that are part of a DBG are required to complete a separate annual report for each member of the DBG. The FSF submits that this involves significant duplication of information and if the requirement was amended to require one annual report for all the entities within a DBG this would result in reduced duplication and compliance costs.

Technical Amendments:

When the AML/CFT Act applies to financial institutions: Amongst the amendments to the AML/CFT Act envisaged by the draft Bill is an amendment to what is presently section 6(a). At present, section 6(a) states that in the case of a reporting entity that is a financial institution, the Act applies only to the extent that "*the financial activities undertaken by that entity fall within the activities described in the definition of financial institution*".

That is clearly drafted, and well understood by FSF members that are financial institutions. However clause 6 of the draft Bill would replace the existing section 6(a) with a new section 6(3)(a) to the effect that the Act would apply to "activities described in the definition of financial institution" only if they also –

> "*may give rise to a risk of money laundering or financing of terrorism*".

The FSF considers that change lacks clarity to an undesirable extent. In particular –

- Who decides whether particular activities "may give rise to a risk of money laundering or financing of terrorism"? That question would be of critical importance to financial institutions but is left unanswered by the draft Bill;

- For instance, would it be permissible for, say, a mortgage lender to conclude that its mortgage loans were unlikely to give rise to any real risk of money laundering, and consequently conclude that the Act did not apply to them?

- Other mortgage lenders might however conclude that their mortgage loans did involve some risk of money laundering, even if only remote, and consequently would comply with the Act. That would result in the same types of financial institutions applying different practices in respect of the same activity, which is clearly undesirable;

- One might have thought that the fact that a number of activities are listed as part of the Act's definition of "financial institution" necessarily involved a Governmental judgement that those activities involve a sufficient risk of money laundering to justify their regulation by the Act, yet the new section 6(3)(a) proposed by the draft Bill suggests otherwise.

As a result, the FSF is concerned that this change could cause real uncertainty as to when or how the AML/CFT Act applies to financial institutions. The proposed change does not seem to be explained in the Information Paper, and it is not clear to the FSF why it is considered necessary.

The FSF would welcome the opportunity to discuss this matter with officials if there is perceived to be a problem with the present text of section 6, but at present the FSF is firmly of the view that this change is undesirably lacking in clarity to such an extent that it should not proceed.

<u>Other Amendments</u>: the FSF also wishes briefly to comment on 3 other points that it has noticed while studying the draft Bill:

a) <u>Definition of "effective administration of the AML/CFT regulatory regime"</u>**:** Clause 5 of the draft Bill will insert a new definition of "effective administration of the AML/CFT regulatory regime" into the Act. Paragraph (a) of that new definition refers to the "regulatory regime". The FSF suggests that reference should be to the "AML/CFT regulatory regime", as it is in the term that is being defined, and also as already used elsewhere in the Act (eg, in section 154(4)(2)(f));

b) <u>Definition of "designated business group"</u>**:** Clause 5(2) of the draft Bill will insert into the Act a new definition of "designated business group". Subparagraphs (vi) – (x) of paragraph (d) of that new definition each refer to entities that are "related". The FSF suggests that it is not clear what that word means in those places, particularly when there are two other definitions of "related" that will apply to other parts of the definition;

c) <u>Prescribed amounts</u>: Clause 5(6) would change the definition of "prescribed transaction", so that it referred to a transaction having a "value equal to or greater" than a prescribed amount, rather than a "value greater" as presently, and Clause 5(5) would make the same change to the definition of "occasional transaction". The FSF assumes that would be accompanied by changes to the relevant prescribed amounts, so that for example in the case of "occasional transaction" the Anti-Money Laundering and Countering Financing of Terrorism (Definitions) Regulations would in future refer to $10,000 rather than to $9,999.99. While the FSF sees the use of round numbers in that way as preferable, it also notes that many internal AML manuals refer to the definition of "occasional transaction" and will need to be changed if what is effectively a 1 cent change proceeds, which will involve some degree of cost.

The FSF trusts that its above responses are helpful, and would be pleased to discuss further, if that would be of assistance.

Lyn McMorran
EXECUTIVE DIRECTOR

Appendix "A " FSF Membership List

<u>Rated</u> Asset Finance (B) Fisher & Paykel Finance (BB+) <u>Non-Rated</u> Mutual Credit Finance Gold Band Finance Limited	BMW Financial Services Branded Financial Services Community Financial Services Go Cars Finance Ltd European Financial Services Mercedes-Benz Financial Services Motor Trade Finance Nissan Financial Services NZ Ltd Onyx Finance Limited Toyota Finance NZ Yamaha Motor Finance <u>Leasing Providers</u> Custom Fleet Fleet Partners NZ Ltd LeasePlan NZ Ltd ORIX NZ SG Fleet	Advaro Limited Avanti Finance Caterpillar Financial Services NZ Ltd Centracorp Finance 2000 Finance Now Future Finance Geneva Finance Home Direct Instant Finance John Deere Financial Latitude Financial Personal Finance Ltd South Pacific Loans The Warehouse Financial Services Group Thorn Group Financial Services Ltd Turners Finance Limited	VEDA Advantage <u>Debt Collection Agencies</u> Baycorp (NZ) Consumer Credit Management Limited Dun & Bradstreet (NZ) Limited	Autosure Protecta Insurance Provident Insurance Corporation Ltd Southsure Assurance	American Express International (NZ) Ltd AML Solutions Buddle Findlay Chapman Tripp EY Finzsoft KPMG PWC SimpsonWestern (Total : 53 members)