



19 August 2010

Financial Services Update

Anti-Money Laundering Discussion Document

Introduction

The Ministry of Justice (**Ministry**) released a consultation document (**Document**) on the implementation of the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (**AML/CFT Act**) on 9 August 2010. The Document is available [here](#). Submissions on the Document are due on **Monday 6 September 2010**. The Document sets out proposed refinements of the options and proposals set out in the Ministry's earlier discussion document released in February. It also contains detailed proposals for an approach to Codes of Practice relating to Customer Due Diligence. At the same time the Ministry has also released its Ministerial Exemptions Policy, setting out the way in which regulatory and Ministerial exemptions will operate. We released a newsletter discussing the release of the Document and the exemption policy on 10 August - that newsletter is available [here](#). In this newsletter we explore a number of the key matters discussed in the Document.

The AML/CFT Act at a glance

The AML/CFT Act is intended to implement New Zealand's international obligations under the Financial Action Taskforce's (**FATF**) 40 general recommendations and nine special recommendations.

The Act imposes a range of obligations (described in more detail below) on "reporting entities". A reporting entity is any entity which meets the Act's very broad definition of a "financial institution", or which is a casino.

FATF's recommendations emphasise the desirability of a "risk based" approach to AML/CFT. This allows individual reporting entities to exercise professional judgment about the areas of their business which present a risk of money laundering, and to allocate resources accordingly.

Customer Due Diligence (**CDD**) obligations are a major aspect of the legislation. New CDD obligations will require significant investment in systems and training by reporting entities that must collect a range of information about their customers when carrying out CDD.

The AML/CFT Act provides for four main types of CDD: simplified, standard, enhanced, and ongoing. Simply put, CDD will be conducted on any new customer (eg account holder), or any non-customer who is carrying out a transaction above a certain threshold. The default for new customers will be the standard CDD process. In principle, lower risk customers and transactions will be subject to the lesser requirements of simplified CDD, while higher risk customers and transactions will be subject to enhanced CDD. CDD obligations will also apply to beneficial owners which may have significant practical implications in respect of trust companies.

Another major obligation under the AML/CFT Act is for reporting entities to undertake risk assessments and to implement compliance programmes based on the risk profile identified. Organisations must also appoint AML compliance officers. Again, those new requirements are onerous and will require considerable resource and expense to be effectively implemented.

Timing

An issue for many reporting entities will be the date that their full responsibilities under the AML/CFT Act will come into force. The Document indicates that a commencement time frame of two years from the gazetting of the regulations is proposed. On the basis of current timeframes for the release of the AML/CFT Act regulations this suggests a commencement date of approximately November/December 2012.

While November/December 2012 appears to be in the distant future, reporting entities need to remember that the 2012 date is when they will be expected to comply in full with their obligations under the AML/CFT Act. Accordingly all of the internal processes which will be required to comply with the AML/CFT Act will need to be up and running before the 2012 date. The development of internal processes necessary to comply with the AML/CFT regime can be a lengthy process and reporting entities' will need to be confident of their ability to comply before the implementation date.

Codes of practice

The AML/CFT Act provides for the creation of codes of practice. The Ministers responsible for the bodies which supervise the implementation of the AML/CFT Act are responsible for developing the codes of practice.

Importantly when a court is called upon to determine whether a reporting entity has complied with the provisions of the AML/CFT Act they are required to have regard to the codes of practice then in force.

The Document makes it clear that codes of practice are not mandatory; they are however intended to set expectations. Reporting entities can opt out of any code of practice, though they must inform their regulator of any decision to do so.

Thresholds

The AML/CFT Act provides for a number of specific thresholds, below which CDD is not required. In setting these thresholds the Document makes it clear that Trans Tasman harmonisation is an important goal for the regulators.

For that reason the document identifies four areas where the Ministry feels harmonisation would be appropriate:

- stored value cards (proposed threshold of \$5,000 non cash and \$1,000 cash);
- money and postal orders (proposed threshold of \$1,000);
- currency exchange (proposed threshold of \$1,000); and
- low value insurance policy exemptions (proposed threshold of \$1,500 for an annual premium or \$3,000 for a single premium).

In each of these areas, the Document has proposed numerical alignment with the Australian thresholds, rather than value alignment which would see the current Australian thresholds converted into New Zealand dollars. The Ministry has sought specific feedback from the industry on this preference, and the limits at which the thresholds have been set.

Beneficial ownership

In addition to the above thresholds, the Document proposes to set the beneficial ownership threshold at 25%. This threshold would mean that any individual who owns 25% of more of a customer, would be subject to the CDD requirements discussed below.

Although submitters proposed thresholds between 20% and 50%, the majority supported the adoption of a 25% threshold. This is also consistent with the Australian regime, as well as the Companies Act 1993.

Exemptions

We discussed the Ministerial exemptions policy document in our newsletter on 10 August, but the Document also details several temporary exemptions for second phase entities. In particular, these exemptions clarify whether or not certain industries are caught under the definition of reporting entity, and therefore whether they would be required to comply with the first phase of regulation. The following industries and/or entities have been granted temporary exemptions:

- The New Zealand Racing Board;
- Real estate agents, lawyers, conveyancing practitioners, or accountants who are otherwise captured by the Financial Transactions Reporting Act;
- The New Zealand Lotteries Commission;
- Persons who provide consumer credit under the Credit Contracts and Consumer Finance Act; and
- Government Agencies and some Crown entities.

In addition, there are several specific exemptions for life insurance and funeral policy providers.

Treatment of Authorised Financial Advisers under the Financial Advisers Act

While Authorised Financial Advisers (**AFA**s) under the Financial Advisers Act (**FAA**) are explicitly captured by the AML/CFT regime a number of exemptions have been proposed.

The Document proposes to explicitly exclude persons who are required to be AFA's from the obligation to comply with the AML/CFT Act to the extent that they arrange for other reporting entities to provide financial services. This exemption will also extend to those people providing financial adviser services to wholesale clients as they are not required to be AFAs. The Document indicates that this limb of the proposed exemption will be limited to advice on category one products e.g. equity securities.

It is also currently proposed to exempt financial advisers from the obligation to conduct ongoing CDD as well as allow for a simplified risk assessment procedure to avoid duplicating obligations imposed under the FAA.

Due diligence and Verification

The AML/CFT Act imposes on Reporting Entities the obligation to collect and verify certain information about their customers. The AML/CFT regime provides for three broad levels of CDD:

- standard due diligence;
- simplified due diligence; and
- enhanced due diligence.

The AML/CFT Act provides for prescribed verification procedures; it is proposed that this function will be carried out through the use of codes of practice as discussed earlier rather than through regulation. Following a considerable number of submissions on the ability of reporting entities to carry out address verification the Document sets out in detail which forms of verification will be acceptable under the Act.

The proposed safe harbour code of practice for verifying the name and date of birth of low to moderate risk customers, using documents, provides for one form of photo ID from the following list:

- a New Zealand passport; or
- a foreign passport, national identity card or other similar document issued by a foreign government or agency of the United Nations and which contains a photograph and signature of the person to whom the document is issued; or
- a New Zealand Certificate of Identity (issued to non New Zealand citizens who are unable to get a passport from their own country or to people with refugee status); or
- a New Zealand Refugee Travel Document; or
- a Firearms License.

Importantly, the above list does not include a New Zealand drivers license. However, a New Zealand drivers license in combination with any one of the following will suffice:

- validation that the information presented on the drivers license is reflected in the National Register of drivers licenses;
- validation that the identity information is reflected in records held by an authoritative source;
- a document issued by a registered bank (e.g. a credit card) or a government agency (e.g. a community services card) that contains the persons name and signature.

If no primary photographic identification is available non photographic forms of identification such as:

- a full New Zealand birth certificate;
- an overseas birth certificate
- a citizenship certificate;
- an overseas citizenship certificate,

can be used in conjunction with any of the following:

- a New Zealand drivers license;
- 18+ card; or
- international driving permit.

The AML/CFT act also provides for the identity of clients to be verified by electronic means. The proposed safe harbour put forward in the Document is not as detailed as those for documentary verification. Nonetheless, a framework for a safe harbour has been put forward. The proposed safe harbour will require Reporting Entities to:

- verify the name of customers from at least two electronic sources;
- verify the date of birth from at least one source; and
- verify address from at least one source.

The AML/CFT Act also requires that reporting entities take steps to satisfy themselves that any address information provided to them by customers in most circumstances this will not be difficult. However, where the majority of transactions are small one off transactions conducted outside of a business relationship or conducted from outside of New Zealand such a requirement could prove onerous.

The Document proposes to address these problems by exempting:

- reporting entities from the requirement to verify the address of non New Zealand residents so long as they can show that they have adequate processes in place to prevent the exploitation of the exemption; and
- casinos from the requirement to verify the address of customers undertaking an occasional transaction (except for currency exchange and money remittance services).

Changes to the standard of Due Diligence

The Document proposes to add a new requirement to the verification process requiring reporting entities to collect the names and dates of birth of the beneficiaries of a trust. Where this is not possible because of the discretionary nature of a trust, reporting entities will be required to identify the nature or class of the beneficiaries of the trust and where practicable the number of beneficiaries.

The Document proposes to allow reporting entities to rely on:

- other reporting entities; or
- anyone who is subject to the Financial Transactions Reporting Act,

to have carried out the beneficial ownership requirements in relation to any trust accounts held by them.

In order to act in reliance on these other reporting entities, the reporting entity must take reasonable steps to satisfy itself that the account is being operated for legitimate purposes and not to obscure the beneficial owner of any trust property. Additionally they need to be comfortable that the facility holder has entered into an agreement with the reporting entity providing the facility to allow them to have access to any information about the identity of the beneficial clients upon demand.

How can we help you?

This newsletter highlights the principal details of the Document. However, there are a broad range of matters which may be of interest to you contained in the Document and in the Ministerial Exemptions Policy. As noted, the Ministry is seeking submissions on the Document by 6 September. Further, the Ministry is also inviting parties to apply for exemptions under the policy from now on. If you have any questions, would like to discuss the affects of the new regime on your business, or would like to discuss the preparation of a submission to the Ministry or an application for an exemption, please contact one of our team members below.

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