

Coversheet: AML/CFT Expiring Regulations

Advising agencies	<i>Ministry of Justice</i>
Decision sought	<i>This analysis has been prepared to inform Cabinet decisions regarding new Anti-money Laundering and Countering Financing of Terrorism (AML/CFT) regulations and substantial policy changes to the existing AML/CFT regulations</i>
Proposing Ministers	<i>Minister of Justice</i>

Summary: Problem and Proposed Approach

Problem Definition

What problem or opportunity does this proposal seek to address? Why is Government intervention required?

New Zealand's Anti-Money Laundering and Countering Financing of Terrorism (**AML/CFT**) regime is a robust, risk-based system that detects and deters money laundering (**ML**) and terrorism financing (**TF**), maintains and enhances New Zealand's international reputation, and contributes to public confidence in the financial system.

At a high level, the AML/CFT regime works by imposing obligations on businesses that undertake activities or provide services to the public that carry a risk of being misused for ML/TF. These businesses are known as **reporting entities**.

The AML/CFT regime came into force in 2013, along with six sets of Regulations¹ that relate to the application of the Act. Due to the changing nature of the ML/TF risk environment, three of these six sets of Regulations were issued with expiry dates to ensure they remain fit for purpose.²

The AML/CFT Definitions Regulations 2011 (**Definitions Regulations**) and AML/CFT Exemptions Regulations 2011 (**Exemptions Regulations**) will expire in the next two years. These Regulations contain critical aspects of the AML/CFT regime. For example, Definitions Regulations provide definitions and thresholds that are necessary for the regime to operate, and Exemptions Regulations exempt classes of transactions or businesses that pose a low risk of ML/TF. If no action is taken, these Regulations would expire, and the AML/CFT regime would not function correctly. We were therefore presented with an opportunity to review these Regulations to ensure that they are still fit for purpose and address any issues that are urgent and suitable to be addressed during this review.³

¹ They are: Anti-Money Laundering and Countering Financing of Terrorism (**Definitions**) Regulations 2011, Anti-Money Laundering and Countering Financing of Terrorism (**Exemptions**) Regulations 2011, Anti-Money Laundering and Countering Financing of Terrorism (**Requirements and Compliance**) Regulations 2011, Anti-Money Laundering and Countering Financing of Terrorism (**Cross-border Transportation of Cash**) Regulations 2010, Anti-Money Laundering and Countering Financing of Terrorism (**Prescribed Transactions Reporting**) Regulations 2016, and Anti-Money Laundering and Countering Financing of Terrorism (**Ministerial Exemption Form**) Regulations 2011.

² These three sets of regulations are: Anti-Money Laundering and Countering Financing of Terrorism (**Definitions**) Regulations 2011, Anti-Money Laundering and Countering Financing of Terrorism (**Exemptions**) Regulations 2011, and Anti-Money Laundering and Countering Financing of Terrorism (**Prescribed Transactions Reporting**) Regulations 2016.

³ The Financial Action Task Force (FATF) conducts peer reviews of each member on an on-going basis to assess levels of implementation of the FATF Recommendations. This is called a FATF mutual evaluation, and it involves the testing of a

(NB: in this Regulatory Impact Assessment, 'Regulations' refers to the regulatory instrument, e.g. the AML/CFT Definitions Regulations 2011, while 'regulations' refers to an individual regulation.)

Proposed Approach

How will Government intervention work to bring about the desired change? How is this the best option?

We have taken the opportunity to review the Definitions Regulations and Exemptions Regulations. We propose three packages of changes to ensure that the AML/CFT regime is functioning correctly with the appropriate regulations in place. They are:

- two substantial changes;
- introducing six new regulations; and
- technical changes/clarifications to the existing Regulations.⁴

Substantial changes (Part B)

The first package contains two substantial changes that we propose be made to the Definitions Regulations and Exemptions Regulations:

- Proposal B: amending Regulation 24A of the Definitions Regulations to prescribe that customer due diligence (CDD) must be conducted before an offer to lease is presented to the lessor for commercial lease transactions. This will substantially reduce the disproportionate compliance burden faced by both the lessor and the real estate agents involved; and
- Proposal C: expanding the definition of "related" under regulation 16 of the Exemptions Regulations to capture other business structures that are of low ML/TF risk but who cannot rely on the current definition

New proposed regulations (Part C)

The second package contains six proposed new regulations that we consider will address urgent issues that we have been aware of:

- Proposal D: including limited partnerships in a designated business group (DBG) to reduce the compliance burden each reporting entity in the group faces, while effectively managing ML/TF risks;
- Proposal E: exempting proven low-risk disbursements from the AML/CFT Act to remove this unintended capture and reduce significant compliance costs for those designated non-financial businesses and professions (DNFBPs);
- Proposal F: providing a limited exemption for reporting entities subject to section 143(1)(a) orders (Commissioner's orders) to avoid inadvertently tipping off a customer that is the

country's anti-money laundering and counter terrorist financing compliance regime against 40 key recommendations that FATF have determined are essential to combating these threats. With the mutual evaluation being currently underway, we anticipate the FATF will make recommendations on how to strengthen New Zealand's AML/CFT regime. These recommendations will be considered as part of the AML/CFT regime's statutory review in 2021, where the Ministry of Justice will be required by section 156A of the AML/CFT Act to review the operation of the provisions of the AML/CFT Act and consider whether any amendments to the AML/CFT Act are necessary or desirable.

⁴ Definitions Regulations, Exemptions Regulations, and one technical change to the AML/CFT (Cross-border Transportation of Cash) Regulations 2010.

subject of a Police inquiry;

- Proposal G: requiring enhanced customer due diligence (ECDD) for companies with nominee directors to reflect the higher ML/TF risk associated with companies that have nominee directors. To implement this new regulation, reporting entities will also be required to obtain from a customer that is a company information as to whether any of its directors or shareholders are nominee directors or shareholders, and if so, the identity of the nominator;
- Proposal H: providing a limited exemption for court-appointed liquidators to address the difficulties court-appointed liquidators have with complying with their AML/CFT obligations; and
- Proposal I: extending the mandatory timeframe for section 59 audits from every two years to every three years, or every four years if the relevant AML/CFT superior determines the risk associated with the entity to be low, to better reflect a risk-based approach.

Technical changes/clarifications (Not in this Regulatory Impact Assessment)

The final package contains proposals that are technical and minor in nature. We have received an exemption from the Regulatory Impact Assessment for these proposals to:

- revoke one redundant regulation; and
- update existing regulations to facilitate technical changes/clarifications to improve the clarity and workability of these regulations.

It also includes proposals to:

- remove the expiry dates of Definitions Regulations and Exemptions Regulations; and
- consolidate the existing AML/CFT Regulations into one single Regulation.

All the technical changes/clarifications are outlined in **Appendix 1**.

Under section 154(2) of the AML/CFT Act the Minister must, before making any recommendation to the Governor General regarding regulations, have regard to:

- the purposes of this Act;⁵
- the risk of money laundering and the financing of terrorism (ML/TF);
- the impact on the prevention, detection, investigation, and prosecution of offences;
- the level of regulatory burden on a reporting entity;
- whether the making of the regulation would create an unfair advantage for a reporting entity or would disadvantage other reporting entities; and
- the overall impact that making the regulation would have on the integrity of, and compliance with, the AML/CFT regulatory regime.

Related to the above, we have applied the following criteria to assess options:

- the effectiveness of the AML/CFT regime to deter and detect ML/TF;
- maintaining the compliance burden associated with the option that is proportionate to the risk of ML/TF; and
- whether it is likely to be practical for reporting entities and supervisors to understand,

⁵ The purposes of the AML/CFT Act are to: detect and deter ML/TF; maintain and enhance New Zealand's international reputation; and contribute to public confidence in the financial system.

implement and monitor.

Having regard to the above, it is clear that allowing the Regulations to expire is not a viable option. This is because the removal of the Regulations would result in the AML/CFT regime ceasing to operate correctly. For example, some vulnerabilities posed by higher risk transactions are mitigated through regulations. In casinos, CDD is required for transactions outside of a business relationship where the value is at or above \$6,000, which is lower than the default threshold of \$10,000.

Not addressing identified issues with the expiring Regulations will result in those issues persisting. Non-regulatory or semi-regulatory options do not effectively or appropriately address the problems identified.

Section B: Summary Impacts: Benefits and costs

Who are the main expected beneficiaries and what is the nature of the expected benefit?

The expected beneficiaries are the government, businesses that have AML/CFT obligations (**reporting entities**), and the general public.

Proposal A is reissuing the expiring Definitions and Exemptions Regulations. Because this means simply re-enacting these existing mechanisms, there is no new benefit resulting from this proposal.

Our proposals to amend the existing regulations and issue new regulations are expected to have the following benefits:

- **Proposal B: amending Definitions Regulations 24A to prescribe the time at which real estate agents must conduct CDD** is expected to reduce the potential for real estate agents to duplicate CDD on the same lessor.⁶ This reduces the compliance burden for both the real estate agents and the lessor to be consistent with a risk-based approach;⁷
- **Proposal C: amending Exemptions Regulations 16 to re-define the meaning of related entities** is expected to benefit related entities who would be able to rely on this exemption but for the fact that they are not bodies corporate (eg, religious orders) by reducing their compliance burden to be proportionate to their ML/TF risk;
- **Proposal D: issuing a new regulation to include limited partnerships in a designated business group (DBG)** is expected to reduce the compliance burden faced by related limited partnerships, who currently cannot form a DBG because of the narrow prescription for DBGs currently provided by the AML/CFT Act;⁸
- **Proposal E: issuing a new regulation to exempt low-risk disbursements** is expected to reduce the compliance burden of DNFBPs who provide low-risk disbursements;⁹
- **Proposal F: issuing a limited exemption for reporting entities subject to a Commissioner's Order¹⁰ or a production order¹¹ from conducting a higher level of CDD** is expected to prevent tipping-off customers who are subject of a Police inquiry, and therefore improve detection and deterrence of ML/TF.
- **Proposal G: issuing a new regulation to require reporting entities to obtain information from companies as to the existence of any nominee directors and shareholders and conduct ECDD on the company** is expected to address a significant vulnerability associated with nominee director relationships in the New Zealand context, and prevent the misuse of nominee directors;
- **Proposal H: issuing a new regulation to provide a limited exemption for court-appointed liquidators** is expected to address the difficulties currently faced by court-

⁶ This is because while multiple real estate agents can represent the same premise to prospective tenants, not all of them would present an offer to the lessor. There is no ML/TF risk if the real estate agents do not present any offer to the lessor.

⁷ Because the risk of ML occurs once a lease is offered/signed, the duplication of CDD and the existing level of compliance burden does not contribute to the mitigation of ML/TF risk.

⁸ Limited partnerships are not able to be a part of a DBG unless they provide a service under a joint venture agreement with other members of the group. This is because limited partnerships are unable to be "related" under the AML/CFT Act since as a legal structure, limited partnerships do not have voting products.

⁹ Such as payments made to the New Zealand Government.

¹⁰ The Commissioner of Police can issue orders under Section 143(1)(a) of the AML/CFT Act to compel the production of all records, documents, or information to Police relevant to an intelligence gathering inquiry as well as share reports generated under the AML/CFT Act.

¹¹ Reporting entities may be required under Subpart 2 "Productions Orders" of the Search and Surveillance Act 2012 to produce documents of a customer who was suspected of committing an offence.

appointed liquidators with complying with the CDD requirements, while ensuring that CDD is conducted for higher-risk customers and services;

- **Proposal I: issuing a new regulation to reduce the mandatory audit frequency from every two years to every three years** to reflect that most reporting entities are of medium ML/TF risk. This is expected to reduce the compliance burden for most reporting entities (who are medium-risk) proportionate to their risk profile.

Overall, these proposals will:

- ensure the compliance burden for reporting entities and transactions is proportionate to ML/TF risk, particularly where the entities/transactions are low risk. Any reduction in compliance burden will reduce the flow-on burden on customers of those reporting entities (Proposals B, C, D, E, H, I);
- address areas of ML/TF vulnerability by reducing the potential for criminals or terrorist financiers to misuse nominee director or nominee shareholder arrangements, and by avoiding tipping off customers that are subject to an inquiry (Proposals F, G); and
- give better effect to the AML/CFT regime's risk-based approach by prescribing audit timeframes that better reflect the reporting entities' ML/TF risk (Proposal I).

It is not possible to quantify the benefits of reducing vulnerabilities within the AML/CFT system that will result from Proposals F and G. We consider that making it harder for nominee director and shareholder relationships to be misused (Proposal G) is likely to increase detection and deterrence of ML/TF as well as enhance New Zealand's international reputation. Similarly, reducing the likelihood of a reporting entity tipping off a suspect to a Police inquiry (Proposal F) will enhance detection and deterrence of ML/TF.

Where do the costs fall?

Four of our proposals are likely to generate costs to government and regulated parties.

Proposal D: issuing a new regulation to include limited partnerships in a designated business group (DBG) is likely to generate costs for the AML/CFT Supervisors, ie, the Department of Internal Affairs (DIA), Financial Markets Authority (FMA), and the Reserve Bank of New Zealand (RBNZ), because the proposed new regulation would require supervisors to process applications from reporting entities who can now rely on this proposal to form a DBG.

The AML/CFT Supervisors have estimated the costs likely to be insignificant and confirmed that they would be absorbed through Departmental baselines. DIA estimates that this would generate a one-off cost of a maximum of approximately \$10,000 maximum in staff time. FMA estimates the costs to be \$10,000 per year in staff time. RBNZ anticipates less than 5 limited partnerships are likely to utilise this proposal and estimates the costs from this proposal to be nominal.

Proposal F: issuing a limited exemption for reporting entities subject to a Commissioner's Order or a production order from conducting a higher level of CDD is likely to generate costs for the Police. As the exemption expires after 30 days, the Police will need to monitor entities subject to Commissioner's Orders and production orders to determine whether an extension of the exemption is required. Police has estimated the cost to be negligible and confirmed that this cost would be absorbed through Departmental baselines.

Proposal G: issuing a new regulation to require reporting entities to obtain information from companies as to the existence of any nominee directors and shareholders and conduct ECDD on those companies is likely to generate costs for reporting entities whose customers are companies with nominee directors. This cost arises from reporting entities being required to obtain

information from companies as to the existence of nominee director or shareholder relationships and then conduct ECDD if these relationships exist. Both reporting entities and those companies will be impacted by this proposal by needing to obtain/provide information about the existence of nominee directors and shareholders and then conduct ECDD if required.

We are unable to ascertain the costs this proposal is likely to generate for those companies because it is currently impossible to determine the number of companies that have nominee directors as their existence is not noted on the Company Register. However, we do not expect providing information as to the existence of nominee directors to be overly onerous as companies are *de facto* required to hold information about the beneficial ownership (including the existence of nominee directors or shareholders) in order to comply with a Registrar's request under sections 365A — 365H of the Companies Act 1993.

Proposal I: issuing a new regulation to reduce the mandatory audit frequency from every two years to every three years is likely to generate costs for AML/CFT Supervisors, as they may request more frequent audits from higher-risk reporting entities, and less frequent audits from lower-risk reporting entities.

The AML/CFT Supervisors have confirmed that these costs would be absorbed through Departmental baselines. DIA estimates that this would generate a one-off cost of approximately \$1,000 to update their IT system to capture the frequency of each entity's audit. DIA also estimated that there would be an ongoing cost of no more than \$5,000 a year in staff time to account for a small level of extra work in risk modelling and identification and communication with entities about their audit frequency. FMA estimates that this would cost at most \$10,000 per year. RBNZ anticipates that only a small number of reporting entities would be required to be subject to either a more frequent or less frequent audit. RBNZ therefore considers that this proposal would have a nominal operational impact and cost on RBNZ.

What are the likely risks and unintended impacts, how significant are they and how will they be minimised or mitigated?

The significant diversity in businesses that have AML/CFT obligations is an inherent challenge for the AML/CFT regime as it can be difficult to ensure that a regulation functions appropriately for every type of captured business. For example, a proposal may function correctly for a bank, but may not function correctly for a real estate agent.

Owing to the nature of the proposals, the impact of this challenge is unlikely to be significant (as no significant changes are proposed). Nevertheless, we have minimised this by consulting with a diverse range of industry stakeholders and peak bodies. In addition, we have ensured that, where possible, proposed changes are not linked to a type of business or business structure. If the impact of this challenge eventuates, it can be mitigated through Ministerial exemptions¹² and the statutory review of the AML/CFT Act scheduled in 2021.

Identify any significant incompatibility with the Government's 'Expectations for the design of regulatory systems'.

There is currently no system stewardship approach to this regulatory area. However, the statutory review of the AML/CFT Act in 2021 will necessarily include a review of the AML/CFT Regulations. Additionally, the National AML/CFT Strategy agreed to by Cabinet [DEV-19-MIN-0270 refers] includes actions for the government to improve private sector engagement with the operation and

¹² Under section 157 of the AML/CFT Act, the Minister may exempt a reporting entity, a class of reporting entities, a transaction or a class of transactions from the requirements of all, or any of the provisions of the Act.

governance of the regime. This will improve the AML/CFT regulatory regime's compatibility with the government's "Expectations for the design of regulatory systems".

Section C: Evidence certainty and quality assurance

Agency rating of evidence certainty?

We consider that there is an adequate evidence base for our analysis of ML/TF risk, informed by the National Risk Assessment, the relevant Sector Risk Assessments and risk assessment by the Ministry as part of the policy process.

We have mostly relied on anecdotal evidence from reporting entities and their supervisors on the analysis of compliance burden, and the workability of our proposals.

To be completed by quality assurers:

Quality Assurance Reviewing Agency:

Ministry of Justice

Quality Assurance Assessment:

The Ministry of Justice has reviewed the Regulatory Impact Assessment and associated supporting material, and consider that the information and analysis summarised in the Regulatory Impact Assessment **meets** the Quality Assurance criteria.

Reviewer Comments and Recommendations:

While there are limits to targeted consultation and full costings are unable to be provided, we note that the risk of imposing unnecessary compliance costs on businesses are mitigated by the existing exemption regime and that the effectiveness of the proposals will be further reviewed during the scheduled statutory review of the AML/CFT Act in 2021. We do not consider these limitations impair the ability of Cabinet to fully rely on the analysis in the Regulatory Impact Assessment for its decision making.

Impact Statement: expiring AML/CFT regulations

Section 1: General information

Purpose

The *Ministry of Justice* is solely responsible for the analysis and advice set out in this Regulatory Impact Statement, except as otherwise explicitly indicated. This analysis and advice has been produced for the purpose of informing key policy decisions to be taken by Cabinet.

Key Limitations or Constraints on Analysis

Limitations and constraints on the analysis in this document include:

- we were only able to test our proposals by way of targeted consultation instead of a public consultation. This limited the pool of people we were able to test our thinking with.
- we have not conducted a full Cost/Benefit Analysis to quantify, in dollar terms, the Net Present Value of the proposals. Costs and/or benefits for businesses, the Crown, and the public have been identified but only estimated in general terms.

Responsible Manager (signature and date):

Lauren McIntosh

Criminal Law, Policy Group

Ministry of Justice

11 March 2020

Section 2: Problem definition and objectives

2.1 What is the context within which action is proposed?

New Zealand's AML/CFT regime is a robust, risk-based system that detects and deters ML and TF, maintains and enhances New Zealand's international reputation, and contributes public confidence in the financial system.

At a high level, the AML/CFT regime works by imposing obligations on businesses that provide activities or services to the public that carry a risk of being misused for ML or TF. These businesses are known as **reporting entities**.

There are three agencies that are appointed in the AML/CFT Act as **AML/CFT Supervisors** to assist reporting entities and take enforcement action against non-compliant reporting entities. They are: Reserve Bank of New Zealand (RBNZ), Financial Markets Authority (FMA), and Department of Internal Affairs (DIA).

The AML/CFT regime came into force in 2013 and was substantially amended in 2017. A number of Regulations have been issued since 2010 to support the operation of the regime. Due to the changing nature of the risk environment, some of these Regulations were issued with expiry dates to ensure they remain fit for purpose and continue to align with New Zealand's ML/TF risk.

New Zealand's ML/TF risk is dynamic and has changed following the development and implementation of the AML/CFT Act. This is shown through several National Risk Assessments and Sectoral Risk Assessments which have observed increases and decreases to ML/TF threats and vulnerabilities, partly as a result of government intervention.

2.2 What regulatory system, or systems, are already in place?

Objectives

The AML/CFT regulatory system was developed to:

- detect and deter ML/TF; and
- maintain and enhance New Zealand's international reputation by adopting, where appropriate in the New Zealand context, recommendations issued by the FATF; and
- contribute to public confidence in the financial system.

Overview of the regulatory system

The AML/CFT regulatory regime consists of the AML/CFT Act which provides for the compliance obligations upon reporting entities as well as outlining the powers and responsibilities for the Ministry of Justice, the AML/CFT Supervisors, the New Zealand Police, and the New Zealand Customs Service.

- the **Ministry of Justice** is the lead policy agency for AML/CFT and administers the Act and associated regulatory instruments.
- the **AML/CFT Supervisors (DIA, FMA, RBNZ)** are responsible for risk-based supervision of reporting entities with their compliance obligations. The AML/CFT Supervisors are also empowered to take enforcement action against reporting entities which do not comply.
- the **New Zealand Police** has three key roles under the AML/CFT regime:

- the Financial Intelligence Unit (FIU) of the New Zealand Police is empowered to receive suspicious activity reports and prescribed transaction reports from reporting entities, as well cross-border cash reports from Customs officers;
 - having a primary law enforcement role — Police is also responsible for investigating and prosecuting ML and TF and performing the asset recovery role on behalf of New Zealand law enforcement and regulatory agencies; and
 - Police has a primary role in preventing, detecting, investigating and prosecuting terrorism activity in New Zealand.
- the **New Zealand Customs Service** is responsible for receiving reports of cross-border transportation of cash and can deal with offences for failures to declare cash moving into or out of New Zealand.

The AML/CFT Act has broad regulation making powers to support the operation of the Act by, for example, prescribing reporting thresholds and forms for reports, as well as including or excluding types of businesses and transactions (sections 153 and 154, generally). Six Regulations have been issued using those powers. The Act also allows for the Minister of Justice to exempt individual reporting entities or classes of reporting entities from all or part of the Act (section 157 of the AML/CFT Act).

The AML/CFT Supervisors can, under section 64, produce Codes of Practice for reporting entities to assist with compliance with obligations under the Act and Regulations. These are approved by the Minister responsible for the supervisor. Codes of Practice have the legal effect of a 'safe harbour', meaning that reporting entities comply with their obligations by complying with the provisions of the Code of Practice.

Finally, both the AML/CFT Supervisors and the New Zealand Police is empowered to issue guidance to assist reporting entities with their obligations under the AML/CFT Act.

Government regulation is the appropriate tool to address the issues identified

Regulation is the appropriate tool for **Proposal B** (amending Definitions Regulations 24A to prescribe the time at which real estate agents must conduct CDD) and **Proposal C** (amending Exemptions Regulations 16 to re-define the meaning of related entities as the issues identified are with existing regulations). Codes of Practice, guidance, or private arrangements would not be able address the relevant issues.

Regulation is also the appropriate tool for **Proposal D** (issuing a new regulation to include limited partnerships in a designated business group), **Proposal G** (issuing a new regulation to require reporting entities to obtain information from companies as to the existence of any nominee directors and shareholders and conduct ECDD on the company), and **Proposal I** (timeframe for section 59 audits). The definition of designated business group provides an exhaustive list of the types of entities as eligible for inclusion, with the ability to prescribe other entities as eligible through regulation (Proposal D). Similarly, the timeframe for section 59 audits is outlined in the AML/CFT Act (Proposal I), with the possibility for regulations to be issued to change the timeframe. Finally, Proposal G imposes a positive obligation upon reporting entities to obtain further information as part of CDD and conduct enhanced CDD on companies with nominee directors. Imposing these compliance obligations can only be done through regulations.

Proposal E (issuing a new regulation to exempt low-risk disbursements), **Proposal F** (issuing a

limited exemption for reporting entities from conducting a higher level of CDD), and **Proposal H** (issuing a new regulation to provide a limited exemption for court-appointed liquidators) could be achieved through issuing a Ministerial class exemption but could not be achieved through non-regulatory means or private arrangements. These proposals require an exemption from obligations. We consider that a regulatory exemption is preferred to a Ministerial class exemption as issuing regulations requires the scrutiny of Cabinet. In addition, Ministerial exemptions must have an expiry date of not more than 5 years (section 159(2)(a) of the AML/CFT Act) which provides less certainty to businesses than a regulation which does not need to expire.

Agencies

The AML/CFT regime has the following agency stakeholders (**AML/CFT Agencies**):

- DIA, FMA and RBNZ as AML/CFT Supervisors;
- New Zealand Police;
- New Zealand Customs Service;
- Ministry of Business, Innovation, and Employment;
- Ministry of Foreign Affairs and Trade; and
- Inland Revenue Department.

Review/assessment

The AML/CFT Act was passed in August 2009 following a comprehensive policy and public consultation process. The Act was substantially amended in 2017 to include designated non-financial businesses and professions (lawyers, conveyancers, accountants, real estate agents, high value dealers, and the Racing Industry Transitional Authority).

A formal Financial Action Task Force (FATF) evaluation of New Zealand's compliance with AML/CFT standards commenced in September 2019. This evaluation will conclude in October 2020 with a public report being adopted by the FATF, which will include recommended actions for New Zealand to improve our AML/CFT regime. Following this, a review of the AML/CFT Act (statutory review) will commence in 2021.

2.3 What is the policy problem or opportunity?

Problem 1: Key AML/CFT Regulations will expire if no action is taken

The Exemptions Regulations and Definitions Regulations will expire in the next two years. These Regulations provide critical aspects of the AML/CFT system, such as exempting classes of transactions or businesses that pose a low risk of ML/TF and providing definitions and thresholds that are necessary for the regime to operate. The AML/CFT regime would cease to function correctly if the Definitions and Exemptions Regulations expired.

Problem 2: Simply reissuing these Regulations is inadequate. Changes are needed to keep the existing regulations up to date and fit for purpose

In the process of considering whether the regulations are still required, we have identified regulations that we consider that should be revoked, clarified, or substantially amended to remain fit for purpose and in line with the changing risk environment. These are discussed in Part B.

Problem 3: Reviewing the Regulations provided us with an opportunity to address new and ongoing issues

Review of the expiring Regulations has provided us with an opportunity to address other issues with straightforward solutions available in regulations. We have identified six issues. They are discussed in detail in Part C.

2.4 Are there any constraints on the scope for decision making?

Some issues raised by submitters fell out of the scope of our review. These issues may be considered during the statutory review of the AML/CFT Act in 2021.

2.5 What do stakeholders think?

The AML/CFT Agencies have been consulted in the development of our proposals. All agencies support the proposals contained in this paper.

We tested our initial thinking by way of a targeted consultation with key stakeholders and peak bodies. We received nineteen submissions from a variety of key stakeholders and industry groups. Submissions were generally very supportive of the proposals. Only our initial proposal of requiring ECDD for companies with nominee directors attracted opposition from three submitters, largely based on concerns about practically identifying those companies. We have since refined our proposal and we consider our current proposal for requiring reporting entities to obtain information as to the existence of nominee directors or shareholders will address this practical concern.

The submitters' views are discussed in detail under the option analysis in section 3.

We contacted Māori industry groups and business associations as part of the targeted consultation and they did not express views on our proposals. We do not consider that our proposals will disproportionately impact Māori.

Section 3: Criteria, options and impact analysis

3.1 What criteria, in addition to monetary costs and benefits, have been used to assess the likely impacts of the options under consideration?

The Ministry has taken into account the mandatory statutory considerations set out in section 154(2) of the AML/CFT Act, which are:

- the purposes of this Act, which are to detect and deter ML/TF; maintain and enhance New Zealand's international reputation; and contribute to public confidence in the financial system;
- the risk of ML/TF;
- the impact on the prevention, detection, investigation, and prosecution of offences;
- the level of regulatory burden on a reporting entity;
- whether the making of the regulation would create an unfair advantage for a reporting entity or would disadvantage other reporting entities; and
- the overall impact that making the regulation would have on the integrity of, and compliance with, the AML/CFT regulatory regime.

Related to the above, we have applied the following criteria to assess the options:

- **Effectiveness at detecting and deterring ML and TF**

How effective the option is at deterring and detecting ML/TF by delivering intelligence to competent authorities or addressing ML/TF vulnerabilities, taking into the account the risk of ML/TF associated with products, services and entities affected by the regulations, and the overall impact that making the regulation would have on the integrity of, and compliance with, the AML/CFT regulatory regime (considering the purposes of the Act);

- **Proportionality**

The extent to which the compliance burden for businesses and the public and the operational cost of the government to ensure compliance is proportionate to the associated ML and TF risk, and where applicable, whether the making of the regulation would create an unfair advantage for a reporting entity or would disadvantage other reporting entities; and

- **Practicality**

The extent to which the option will be easy for businesses and government agencies to understand, implement, and monitor.

Assessing the options against these criteria, in addition to the statutory considerations, reflect the "Government Expectations for Good Regulatory Practice." It ensures the proposed changes are in line with the ML/TF risk, proportionate in the way it treats regulated parties, and practical for both the regulated parties and the regulators.

These criteria are interlinked. For example, a proportionate and practical approach will enhance the effectiveness of the overall AML/CFT regime. A more effective regime will better achieve the purposes of the Act: detection and deterrence of ML/TF, maintaining and enhancing New Zealand's

international reputation, and contributing to public confidence in the financial system.

More specifically, the substantive changes and four of the proposed new regulations will ensure the compliance burden on reporting entities is proportional to ML/TF risk without negatively impacting ML/TF detection and deterrence. Proportional compliance burdens will contribute to public confidence in the financial system and maintain the integrity of the AML/CFT regime overall. The proposed changes are also consistent with New Zealand's international obligations.

The other two proposals for new regulations will increase the regime's effectiveness at detecting and deterring ML/TF. While one proposal is expected to increase compliance costs for businesses, we consider these costs are proportional to the associated ML/TF risk. They will also assist with the prevention, detection, investigation, and prosecution of offences.

The proposals are informed by, and consistent with, the National AML/CFT strategy, which is to maintain the integrity and stability of the financial system and in doing so contribute to a safe, healthy and prosperous New Zealand and strong international reputation. Cabinet agreed to this strategy in October 2019 [DEV-19-MIN-0270 refers].

3.2 Option analysis

Part A: The Exemptions Regulations and Definitions Regulations are expiring

A.1 What is the policy problem or opportunity?

The Exemptions Regulations and Definitions Regulations will expire in the next two years. These Regulations provide critical aspects of the AML/CFT system, such as exempting classes of transactions or businesses that pose a low risk of ML/TF and providing definitions and thresholds that are necessary for the regime to operate. For example:

- a number of low risk reporting entities, transactions, and services are currently exempt through regulations because they carry low ML/TF risks.
- vulnerabilities posed by higher risk transactions are mitigated through regulations. For example, in casinos, CDD is required for transactions outside of a business relationship where the value is at or above \$6,000, which is lower than the default threshold of \$10,000.

Vulnerabilities, such as the example above, that are currently mitigated would no longer be mitigated if the Regulations are allowed to expire. Furthermore, if these Regulations expired, many previously exempted reporting entities would be required to comply with the AML/CFT Act. This compliance burden would not be justified by the ML/TF risk.

A.2 What options have been considered?

Three options have been considered. They are:

Option 1: No action taken, and allow the regulations to expire

This means these Regulations will expire on their respective expiry dates. They will not be reissued.

Option 2: Reissue Regulations without any changes (status quo of the regulations)

This option avoids exposing New Zealand to ML/TF vulnerabilities and suddenly subjecting a significant number of low risk reporting entities, transactions, and services to the AML/CFT obligations that they are currently exempt from. It, however, does not provide us with the opportunity to update the Regulations to ensure their workability, and that they are still fit for purpose and in line with the risk environment.

Option 3: Reissue Regulations with changes to improve the overall AML/CFT regime (preferred)

As with option 2, this will avoid the possibility of the AML/CFT regime no longer working. Reissuing these Regulations with changes will provide an opportunity to review these regulations and determine whether any changes are required. It will also provide an opportunity to address issues with the clear and simple solutions available in regulations.

A.3 Stakeholders' view

All stakeholders consider that the regulations should not be allowed to expire.

A.4 Impact analysis			
	Option 1: No action taken, and allow the Regulations to expire	Option 2: Reissue Regulations without any changes (status quo)	Option 3: Reissue Regulations with changes to improve the overall AML/CFT regime (preferred)
Effectiveness at detecting and deterring ML/TF	<p style="text-align: center;">--</p> <p>Some regulations prescribe lower thresholds for reporting entities that are of higher ML/TF risk than the ones provided by the Act (eg, the applicable threshold value for occasional transactions is \$10,000, but thresholds for cash transaction in casino is \$6,000). Allowing these regulations to expire would result in ML/TF vulnerabilities associated with those higher-risk entities and transactions no longer being addressed.</p>	<p style="text-align: center;">0</p> <p>This is insufficient in addressing some vulnerability that we have identified (eg, companies with nominee directors). For example, companies that have a nominee director relationship present a higher ML/TF risk, but we currently do not have any measure in place to prevent the misuse of nominee directors.</p>	<p style="text-align: center;">++</p> <p>This option would preserve these thresholds and would maintain the current levels of effectiveness at ML/TF detection and deterrence. In addition, it would allow us to identify ML/TF vulnerabilities that could be addressed through changes to the existing regulations or issuing new regulations.</p>
Proportionality	<p style="text-align: center;">--</p> <p>Some regulations exempt lower-risk reporting entities from certain obligations under the Act. Allowing these regulations to expire would, in effect, impose compliance burden on these reporting entities, which are disproportionate to their ML/TF risk. In addition, higher ML/TF risk transactions would no longer attract higher compliance obligations (which is proportionate to the risk).</p>	<p style="text-align: center;">0</p> <p>Reissuing the Regulations without any changes is unable to address certain proportionality issues that we have identified. For example, the current drafting of Exemptions Regulation 16 does not include services provided between related religious orders, which are of lower ML/TF risk (services provided between entities that are related carry a lower ML/TF risk).</p>	<p style="text-align: center;">++</p> <p>This would maintain the current levels of proportionality provided by exemptions, exclusions, and inclusions. It would also provide us an opportunity to better achieve proportionality by making changes to the existing regulations or issuing new regulations.</p>
Practicality	<p style="text-align: center;">--</p> <p>Allowing regulations (eg, regulations that clarify who are reporting entities under the Act) to expire would cause uncertainties among reporting entities and government agencies.</p>	<p style="text-align: center;">0</p> <p>Reissuing the Regulations without any changes preserves the level of practicability of the existing regulations, however, it is insufficient in improving these regulations to ensure that they are easy for reporting entities and supervisor to understand, implement, and monitor.</p>	<p style="text-align: center;">++</p> <p>Reissuing the Regulations with necessary changes allows us to make sure that the regulations are easy for reporting entities and supervisors to understand, implement and monitor.</p>
Overall	<p style="text-align: center;">--</p>	<p style="text-align: center;">0</p>	<p style="text-align: center;">++</p>

Part B: Regulations identified as requiring substantive changes

(B) Definitions Reg 24A – Time at which real estate agents must conduct customer due diligence

B.1 What is the policy problem or opportunity?

This regulation prescribes that, for real estate agents, customer due diligence (CDD) must be conducted before a real estate agent enters into an agency agreement. This policy was based on the understanding that real estate agents generally have exclusive agency agreements when selling real estate.

However, when conducting commercial lease transactions (which is captured in the scope of real estate agency work), real estate agents rarely have exclusive agency agreements with respect to the lessor. Most properties are offered for lease under a general agency arrangement, where all involved agents can represent the premises to prospective tenants. The current drafting of this regulation requires all those agencies to conduct CDD on the lessor when they entered into the general agency arrangement. Consequently, the same lessor could have had CDD conducted on them multiple times. This imposes unnecessary burden on the real estate agents and the lessors, because not all agencies will present an offer to the lessor.

B.2 What options have been considered?

Three options have been considered. They are:

Option 1: Renew this regulation without any changes (status quo)

This means that real estate agents will continue to be required to conduct CDD on the lessor before they enter into an agency agreement.

Option 2: Prescribing that CDD must be conducted before the commercial lease transaction is conducted

This would mean that real estate agents are required to conduct CDD at the time before the commercial lease transaction is conducted. Because there are many possible points at which a commercial lease could be said to be “conducted”, we recognise that this option may lead to potential inconsistency and uncertainty across the sector.

Option 3: Prescribing that CDD must be conducted before an offer to lease is presented to the lessor (preferred)

This would require real estate agents to conduct CDD before they present an offer to lease to the lessor in commercial leasing situations. This would make it clear the exact capture point real estate agents are required to conduct CDD.

B.3 Stakeholders’ view

Our initial proposal was to amend the regulation to prescribe that CDD must be conducted before the commercial lease transaction is conducted. There was general support for this approach from submitters.

Two submitters proposed that our initial proposal should apply to all real estate transactions. We do not consider our preferred option should apply to all real estate transactions. This is because the policy for bringing the real estate sector under the AML/CFT regime is still quite new. Not enough

time has lapsed for us to test and determine if similar issue exists for all real estate transactions, and if it warrants an amendment to the regulation to address the issue.

One submitter proposed option 3. After carefully considering this proposal, we recognised that our initial proposal may lead to potential inconsistency and uncertainty across the sector because of the lack of clarity around when a commercial lease could be said to be “conducted”. Option 3 is our preferred option because it provides a clear capture point, which we anticipate will ensure consistency across the sector while also appropriately managing the ML/TF risk associated with commercial lease transactions.

All other AML/CFT agencies support our preferred option.

B.4 Impact analysis			
	Option 1: status quo	Option 2: CDD when commercial lease transaction is conducted	Option 3: CDD before an offer to lease is presented to the lessor (preferred)
Effectiveness at detecting and deterring ML/TF	0	- This option may lead to potential inconsistency and uncertainty across the sector because there are many possible points at which a commercial lease could be said to be “conducted”. This creates the possibility for “weak links” (ie inconsistent practice among real estate agents when conducting CDD), which undermines the deterrence effect of the AML/CFT regime	0 This option achieves approximately the same level of effectiveness of detecting and deterring ML/TF as the status quo.
Proportionality	0	0 Compared to the status quo, this option would reduce the potential duplication of CDD, and therefore reduce the burden on real estate agents and their customers. However, given the uncertainty around the time where a commercial lease is “conducted”, this option would likely require further guidance/assistance from the supervisor for the real estate sector, DIA. This would increase burden on DIA.	+ This option reduces the potential for CDD to be duplicated and therefore reducing the overall compliance burden of reporting entities and their customers to be proportionate to their ML/TF risk, as the opportunity for ML occurs once a lease is offered/signed.
Practicality	0	- Given there are many possible points at which a commercial lease could be said to be “conducted”, this option may lead to inconsistency and uncertainty across the real estate sector, which would not be easy for businesses and government agencies to understand, implement, or monitor.	+ As the offer to lease is a clearly defined point in the commercial lease transaction, this option is easily implemented.
Overall	0	-	+

(C) Exemptions Reg 16 – Exclusions: relevant services provided to related entities

C.1 What is the policy problem or opportunity?

This regulation wholly exempts services provided between a reporting entity and a customer where the reporting entity and the customer are “related”. This exemption exists because services provided between entities that are related carry a lower ML/TF risk.

The current drafting of this regulation relies on the meaning of “related” as provided in section 12 of the Financial Markets Conduct Act 2013 (FMCA). This definition requires the reporting entities and the customer to both be a body corporate with voting products in order to be “related”. This therefore excludes legal persons without voting products or shares (eg incorporated societies) and legal arrangements (eg trusts and partnerships).

Consequently, reporting entities who provide services to related entities that are not bodies corporate but are of low ML/TF risk and only provide services intra-group are inadvertently left out by this exemption. These reporting entities have turned to Ministerial exemption application for regulatory relief from the Act. This has resulted in a substantial amount of resource-intensive Ministerial exemption applications. To date, we have received 7 individual Ministerial exemption applications from 5 reporting entities. All but one has been granted a Ministerial exemption.¹³ These applications sought for a full exemption from the Act for services:

- provided by the diocese to parishes, Churches, schools, chaplaincies, religious orders and other church entities under the common control of the diocese, or
- provided by one entity to other related entities, who are all under the control of a third party.

These services would have been exempt from this regulation but for the fact that these various church entities are not body corporates related within the meaning of section 12(2) of the FMCA.

C.2 What options have been considered?

Option 1: Renew this regulation without any changes (status quo)

This option would continue exempting services between a reporting entity and a customer where the reporting entity and the customer are “related”, as defined under section 12 of the FMCA.

Option 2: Expand the concept of “related” to include entities where Entity A is ‘controlled’ by Entity B (or vice versa) or where A and B are ‘controlled’ by C and define “control”

This would re-define the concept of “related” to include entities that are in partnership as well as entities where A is “controlled” by B (and vice versa), or where A and B are both “controlled” by C. This would mean that services provided within a corporate structure in the following scenarios would be exempt from the Act:

- where the customer and the entity providing the service are related bodies corporate;
- where the customer is **controlled** by the entity providing the service;
- where the entity providing the service is **controlled** by the customer;
- where a third entity **controls** both the customer and the entity providing the service;
- where the customer and the entity providing the service is a partnership.

¹³The Ministerial exemption application that has not been granted is currently with the Associate Minister of Justice for consideration.

This option includes defining control to ensure certainty to both the AML/CFT Supervisors as well as reporting entities as to when they can rely on this exemption. We consider “control” may be defined as **“having the capacity to determine the outcome of decisions about the entity’s financial and operational policies”**, which is the definition provided in Schedule 1, clause 48 of the Financial Markets Conduct Act. Providing a definition of “control” would improve the workability of this option.

Option 3: Amend the definition of “related” by replacing “related” with “associated” as defined in the FMCA

As with option 2, this would amend and expand the scope of “related” by replacing “related” with “associated” as defined in the FMCA. This would exempt, for example, where Entity A acts, or is accustomed to act, in accordance with the wishes of Entity B (or vice versa); or where A is able, directly or indirectly, to exert a substantial degree of influence over the activities of B (or vice versa). However, it would also provide an exemption where A is a director or senior manager of B, or whether there is another person with which A and B are associated.

Compared to option 2, we consider this option is likely to have unintended consequences because its scope has potential to be far wider than intended by this regulation. For example, it is possible for entities who do not belong to a same group to rely on “associated” and thereby this exemption.

C.3 Stakeholders’ views

All submissions received support expanding the definition of “related” to give better effect to the original policy intent by exempting services provided wholly within a group of related entities and without an external customer.

All other AML/CFT Agencies support our preferred option.

C.4 Impact analysis			
	Option 1: status quo	Option 2b: exempt services provided between ‘controlled’ entities and define ‘control’ (preferred)	Option 3: amend the definition of “related” by replacing “related” with “associated” as defined in the FMCA
Effectiveness at detecting and deterring ML/TF	0	0 This option achieves approximately the same level of effectiveness of detecting and deterring ML/TF as the status quo, as services provided between related reporting entities are of low ML/TF risk.	-- Because of the wide scope of “associated”, it is possible for entities who do not belong to a same group to rely on “associated” and thereby this exemption. This option is therefore likely to exempt reporting entities that are not necessarily low-risk. It therefore would negatively impact the ability of the regime to detect and deter ML/TF
Proportionality	0	++ This would reduce the compliance burden of entities who are related but for the fact that they are not body corporates related within the meaning of section 12(2) of the FMCA. This would better reflect low ML/TF risk nature of services provided between related entities. This would also reduce the time and resources of supervisors and the Ministry as they would not be required to process as many individual Ministerial exemptions.	- This option has the potential to exempt reporting entities that may not be low risk, and therefore reducing their compliance burden to a degree that is disproportionate to their associated ML/TF risk. This option has the potential of exempting a wide range of reporting entities, which may not be of low ML/TF risk. In those scenarios, a certain degree of compliance burden is justified by their level of ML/TF risk. An exemption therefore is not justified.
Practicality	0	+ This option would be much easier for government agencies to implement as there will be less ministerial exemption applications from reporting entities who are related but for the fact that they are not body corporates related within the meaning of section 12(2) of the FMCA.	0 This option achieves approximately the same level of practicality as it provides a clear definition of “associated”.
Overall	0	+	--

Part C: Proposed new regulations

(D) Including limited partnerships in a designated business group

D.1 What is the policy problem or opportunity?

A designated business group (DBG) allows related reporting entities to pool resources and reduce their compliance burden where they are operating in a larger group of entities as a collective. The Act treats the DBG effectively as a single reporting entity for most compliance obligations. This can significantly reduce the compliance burden each reporting entity faces because a member of a DBG can rely on another member to carry out some obligations on their behalf as set out in section 32 of the AML/CFT Act. These include:

- CDD;
- parts of an AML/CFT compliance programme – such as record keeping, account monitoring and ongoing CDD;
- submitting annual reports on behalf of another member of the DBG;
- risk assessments;
- suspicious activity reporting; and
- prescribed transaction reporting.

Forming a DBG requires each entity in the group to be related to the other entities. This is the key criterion, and as such the AML/CFT Act narrowly prescribes the ways in which reporting entities can be related. This helps reduce the risk that DBGs will be misused by non-compliant reporting entities and increase ML/TF risks overall. Relatedness can be satisfied if the reporting entities carry out a similar business (and therefore face similar risks) or if the reporting entities are part of a broader corporate ownership structure.

Limited partnerships are not able to be a part of a DBG unless they provide a service under a joint venture agreement with other members of the group. However, they are unable to be included in a DBG where the other members are related by ownership of voting products (eg a holding company with subsidiaries). This is because limited partnerships, as a legal structure, do not have voting products.

D.2 What options have been considered?

Option 1: Status quo (no action taken)

This means that no action will be taken to address the issue we identified above.

Option 2: Introduce a new regulation to allow related limited partnerships to form a DBG (preferred)

This would prescribe, in regulations, that related limited partnerships are eligible for inclusion in a DBG.

D.3 Stakeholders' views

Almost all submissions were in support of the proposal, with one submission neutral on the proposal.

Several submitters also suggested allowing other types of corporate entities and relationships to be eligible for inclusion in a DBG, specifically:

- special purpose vehicles established for residential mortgage-backed securities (SPVs);

- law firms operating ordinary partnerships;
- entities in franchise arrangements; and
- all other corporate forms, including charities and trusts.

Considering the policy intent and the need for relatedness to be tightly constrained to effectively manage ML/TF risks, we do not recommend declaring these other forms as eligible at this stage. The SPV identified by a submitter can be included in a DBG through a different eligibility criterion, and law firms operating as ordinary partnerships are already eligible for inclusion.

We do not recommend declaring entities operating under a franchise model as eligible to form a DBG as it potentially carries significant risks for the AML/CFT system. Franchisees are typically independent entities that have purchased the rights to use the franchisor's business logo, name, and operating model. There is no guarantee that the entities involved will face the same ML/TF risks to justify sharing compliance obligations, and the degree of control and influence between the franchisor and franchisee can vary considerably.

Finally, allowing all other corporate forms (including charities and trusts) to form a DBG would require considerable policy work that is not possible at this stage. This policy change would require agencies to consider all possible combinations of corporate entities and whether the entities are sufficiently related to justify sharing of compliance obligations. We recommend considering this issue during the statutory review of the AML/CFT Act in 2021.

All other AML/CFT agencies support our preferred option.

D.4 Impact analysis		
	Option 1: status quo	Option 2: introduce a new regulation to allow related limited partnerships to form a DBG (preferred)
Effectiveness at detecting and deterring ML/TF	0	0 This option achieves approximately the same level of effectiveness of detecting and deterring ML/TF as the status quo, as there is a low risk that these DBGs would be misused by non-compliance companies given the requirement for relatedness.
Proportionality	0	+ This would provide compliance relief for those related limited partnerships. However, it may result in more applications for DBGs and therefore a degree of supervisory burden for the AML/CFT Supervisors. ¹⁴ At the same time though, it may reduce their supervisory burden as they would only need inspect the DBGs rather than the individual members. The prospect of not being required to process the amount of ministerial exemption applications from those reporting entities reduces the operational burden of supervisors, FIU and the Ministry. Further, the slight increase in costs to supervisors is more than offset by the reduction in compliance burden and costs to reporting entities. Overall, therefore, the impact is positive.
Practicality	0	+ Prescribing that limited partnerships can be included in a DBG will be easy for reporting entities and supervisors to understand and implement.
Overall	0	+

¹⁴ As discussed in table 5.2, this impact is insignificant.

(E) Exempting low-risk disbursements

E.1 What is the policy problem or opportunity?

The AML/CFT regime treats monies paid in advance to a designated non-financial business or profession (DNFBP), such as a lawyer, as managing client funds (a captured activity). This includes where the money is paid to the DNFBP for a disbursement, where the DNFBP pays a third party for services or goods provided to the client, such as for filing applications on behalf of the client. Upon receipt of this money, the DNFBP is required to conduct CDD on the client and cease acting if CDD cannot be conducted.

However, the impact of disbursements being captured as managing client funds is that the DNFBP would be obligated to conduct CDD on their client once the funds are received. Further, the DNFBP would be required to cease acting for the client if CDD cannot be satisfactorily conducted. Some DNFBPs are only captured in the AML/CFT regime due to receiving payments in advance.

Furthermore, the ML/TF risk associated with disbursements varies. Some disbursements carry little ML/TF risk, such as payments to the New Zealand government. Others, such as payments to third parties with no apparent relation to the underlying service provided likely carry a higher ML/TF risk. This risk also varies depending on where the third party is located: a payment to a third party in New Zealand is less risky than a payment to a third party in a jurisdiction with insufficient AML/CFT controls or proximate to an active terrorism threat.

The type of DNFBP making the payment to the third party can influence the level of risk. Trust and company service providers (TSCPs) are a type of DNFBP that can receive disbursements and manage client funds. TSCPs have been assessed by DIA as having high inherent ML/TF risk. By comparison, lawyers and accountants have a lower (medium-high) inherent risk.

E.2 What options have been considered?

Option 1: Status quo

This option means no action will be taken to address the issue identified above.

Option 2a: Exclude disbursements for New Zealand government departments, New Zealand Police or local authorities as “managing client funds”

This would exempt from the scope of “managing client funds” money paid to a reporting entity for the purpose of the reporting entity paying to government departments. This would exclude payments of Court fees, application fees, and fees for registration of security interests which is likely to be a significant portion of disbursements received.

Option 2b: Exclude disbursements for barristers, expert witnesses, and professional mediators and adjudicators who carry out businesses in New Zealand as “managing client funds”

This would exempt from the scope of “managing client funds” money paid to a reporting entity for the purpose of the reporting entity paying to a specific service provider, ie a barrister, expert witness, and professional mediator and adjudicator carrying out its business in New Zealand.

There are restrictions on who can provide these services in New Zealand (eg an expert witness needs to demonstrate their expertise), and these disbursements are incurred in relation to an underlying proceeding. As such, we consider these disbursements also carry low ML/TF risk. However, this exclusion would only apply to services provided in New Zealand, as there is less

assurance that providers of equivalent services in other jurisdictions are subject to the same controls.

Option 2c: Exclude all other disbursements intended for all third parties carrying out business in New Zealand where the value of the transaction, or series of transactions, is less than \$1,000 as “managing client funds”

This would exempt from the scope of “managing client funds” money paid to a reporting entity for the purpose of the reporting entity paying to a third party, where the payment is less than \$1,000. This option excludes in the scope payment for disbursements for services provided in other jurisdictions.

We consider that a \$1,000 threshold strikes the appropriate balance between the ML/TF risk of disbursements and compliance costs. This limb would only apply to third parties carrying out business in New Zealand: payments for third parties carrying out business in other jurisdictions are inherently higher risk and should remain included.

Option 3: Combination of option 2a, 2b and 2c (preferred)

This option would best achieve a risk-based approach. It would exclude the types of low-risk disbursements that we have identified, which are:

- Disbursements for New Zealand Government departments, New Zealand Police, or local authorities;
- Disbursements for barristers, expert witnesses, and professional mediators and adjudicators carrying out business in New Zealand; and
- All other disbursements intended for all third parties carrying out business in New Zealand where the value of the transaction, or series of transactions, is less than \$1,000.

Option 4: A “default-out” approach to only include high-risk disbursements

This would exempt all disbursements from the AML/CFT Act, and specifically include disbursements that carry high ML/TF risk. This would require us to identify all high-risk disbursements.

Options not considered:

We have not considered exempting payments for disbursements for services provided in other jurisdictions. This is because payments for services provided by third parties carrying out businesses in other jurisdictions are inherently higher risk.

We have not considered higher thresholds (\$5,000, \$10,000 etc) because we consider the a threshold higher than \$1,000 does not effectively manage the ML/TF risk.

E.3 Stakeholders’ views

All submissions received for the proposal were in support of our preferred option. However, two submitters also disagreed with the interpretation that disbursements are captured as managing client funds.

All other AML/CFT agencies support our preferred option.

E.4 Impact analysis

	Option 1: status quo (no action taken)	Option 2: Excluding low-risk disbursements			Option 3: Combination of option 2a, 2b and 2c (preferred)	Option 4: A “default-out” approach to only include high-risk disbursements
		Option 2a: Exclude disbursements for New Zealand government departments, New Zealand Police or local authorities as “managing client funds”	Option 2b: Exclude disbursements for barristers, expert witnesses, and professional mediators and adjudicators who carry out businesses in New Zealand as “managing client funds”	Option 2c: Exclude all other disbursements intended for all third parties carrying out business in New Zealand where the value of the transaction, or series of transactions, is less than \$1,000 as “managing client funds”		
Effectiveness at detecting and deterring ML/TF	0	0 No impact on detecting or deterring ML/TF as the exemption only applies to low-risk disbursements.	0 No impact on detecting or deterring ML/TF as the exemption only applies to low-risk disbursements.	0 No impact on detecting or deterring ML/TF as the exemption only applies to low-risk disbursements.	0 No impact on detecting or deterring ML/TF as the exemption only applies to low-risk disbursements.	-- Because it is difficult to specify all high-risk disbursements for inclusion, there will be risk creating further vulnerabilities within the system if we are unable to exhaustively identify all high-risk disbursements that should be included.
Proportionality	0	+ This would ensure a better alignment to the risk-based approach.	+ This would ensure a better alignment to the risk-based approach.	+ This would reduce the compliance burden on reporting entities who receive low-risk disbursements. This is more proportionate to the ML/TF risk receiving low-risk disbursements presents.	++ Combining the three options would be the most proportionate approach to a risk-based approach.	- There is a risk that high-risk disbursements may also be exempt under this approach as well as medium-risk disbursements. An exemption would not be justified in light of their associated ML/TF risk.

Practicality	0	+ This would clarify the scope of the requirement of “managing client funds”. Issuing specific conditions for this exemption would assist the monitoring and implementation of this exemption.	+ This would clarify the scope of the requirement of “managing client funds”. Issuing specific conditions for this exemption would assist the monitoring and implementation of this exemption.	+ This would clarify the scope of the requirement of “managing client funds”. Issuing specific conditions for this exemption would assist the monitoring and implementation of this exemption.	+ This would clarify the scope of the requirement of “managing client funds”. Issuing specific conditions for this exemption would assist the monitoring and implementation of this exemption.	- We anticipate the difficulties surrounding specifying all high-risk disbursements for inclusion would make the implementation of this option problematic.
Overall	0	+	+	+	++	--

(F) Providing a limited exemption for reporting entities subject to a Commissioner’s Order or a production order

F.1 What is the policy problem or opportunity?

The Commissioner of Police can issue orders under section 143(1)(a) of the Act, known as a “Commissioner’s Order”. These orders compel reporting entities to produce all records, documents, or information to Police relevant to an intelligence gathering inquiry as well as share reports generated under the AML/CFT Act. Similarly, reporting entities may be required under Subpart 2 “Productions Orders” of the Search and Surveillance Act 2012 to produce documents of a customer who was suspected of committing an offence.

However, there is a risk that a reporting entity may inadvertently “tip off” the customer upon receipt of a Commissioner’s Order or a production order by applying the CDD requirements. “Tipping off” lets the individual concerned know that they are a subject of an inquiry which would make the detection, investigation, and prosecution of any offences difficult, if not impossible).

When a reporting entity receives a Commissioner’s Order or a production order in respect of a customer, the reporting entity may consider that the customer now presents a higher risk than when originally assessed. If that conclusion is reached, the reporting entity is required to re-assess the level of CDD conducted and decide to conduct a higher level of CDD. However, if the customer has already been subject to CDD, being subjected to a higher level of customer due diligence may “tip off” the customer to them being the subject of a Police inquiry.

F.2 What options have been considered?

Option 1: Status quo

This option means no action will be taken.

Option 2: Issue a regulation that exempts reporting entities subject to Commissioner’s Orders or production orders (preferred)

This would provide a limited exemption from CDD for entities subject to the Commissioner’s Orders or a production order. In practice, this means that reporting entities would be exempt from conducting a higher level of CDD in respect of the subject of the Commissioner’s Order or a production order, and would last for a period of 30 days, unless otherwise notified by the Police.

To ensure this option is practical, the supervisors and the Police will work together to develop guidance to support this exemption and address the practical questions raised by submitters during the targeted consultation, such as who is responsible for monitoring the expiry of the order.

F.3 Stakeholders’ views

We have included “a production order” in the scope of this proposed exemption following consultation with the other AML/CFT agencies.

All submissions were in support, with some submitters noting practical considerations such as who is responsible for monitoring the expiry of the order. To ensure the workability of this option, the supervisors and the Police would work to develop guidance to support this exemption and address these practical questions raised by submitters during the targeted consultation.

All other AML/CFT agencies support our preferred option.

F.4 Impact analysis		
	Option 1: status quo (no action taken)	Option 2: Issue a regulation that exempts reporting entities subject to Commissioner's Orders or production orders (preferred)
Effectiveness at detecting and deterring ML/TF	0	<p style="text-align: center;">+</p> <p>This would avoid the potential of tipping off customers who are the subject of the Police inquiry, and therefore enable better detecting and deterring of ML/TF.</p> <p>It is worth noting that this proposal does not prohibit reporting entities from conducting ECDD on customers who are the subject of a Police inquiry. This is because prohibiting ECDD where a customer is the subject of a Police inquiry requires changes to the AML/CFT Act. There is, therefore, still some residual risk of tipping off. Despite this, given that ECDD is potentially costly, we anticipate that reporting entities are unlikely to conduct ECDD if they are exempted from being required to do so.</p>
Proportionality	0	<p style="text-align: center;">0</p> <p>A limited exemption from an ECDD is disproportionate to the high ML/TF risk associated with customers who are the subject of a Police inquiry. However, this exemption mitigates a more significant ML/TF risk by reducing the potential risk of tipping off those high-risk customer</p>
Practicality	0	<p style="text-align: center;">-</p> <p>We expect some reporting entities may need guidance/assistance to understand that this proposal does not prohibit them from conducting a higher level of CDD. The supervisors and the Police would work to develop guidance to support this exemption and address these practical questions raised by submitters during the targeted consultation.</p>
Overall	0	<p style="text-align: center;">+</p> <p>We consider the overall impact to be positive, as the benefit of enabling better detecting and deterring ML/TF outweighs the costs of guidance.</p>

(G) Requiring reporting entities to obtain information from companies as to the existence of any nominee directors and shareholders and the identity of the nominator

G.1 What is the policy problem or opportunity?

Companies that have a nominee director relationship present a higher ML/TF risk. Nominee directors can be established either formally or informally and involve the nominee director and the person providing the instructions (nominator). Nominee director relationships can be misused to obscure the beneficial owner, ie the person who effectively controls the company. The nominee director is the individual listed on the Company Register, while the beneficial owner is not.

A formal nominee director relationship can be established by, for example, the nominee providing the nominator with a Power of Attorney in respect of their director's powers. An informal nominee director relationship exists where the nominee director acts on the instructions of the nominator. These relationships tend to be of a personal, rather than professional, nature (eg the spouse or other family member of the nominator).

Providing nominee director services is legal in New Zealand and there are many legitimate uses for nominees. Despite this, nominee directors are a significant vulnerability in New Zealand with numerous instances of nominee director relationships being misused to facilitate ML and other offending.¹⁵

We do not have any measures in place to prevent the misuse of nominee directors. This is inconsistent with the FATF recommendations, which require all jurisdictions to put measures in place to ensure nominee directors are not misused. These measures could include requiring nominee directors to disclose the identity of their nominator and this information be included on a register or requiring nominee directors to be licensed.

G.2 What options have been considered?

Option 1: Status quo

This option means that no measure will be adopted to address the vulnerability nominee directors pose. This does not address the issue identified above.

Option 2(a): Require companies with nominee directors to be subject to ECDD

This option would introduce a new regulation under section 153(a) which requires ECDD to be conducted on customers which are companies with nominee directors.

This option, compared to option 2(b), does not impose a positive obligation on reporting entities to obtain information from companies as to the existence of nominee directors or shareholders. We therefore consider this option not practical or workable for reporting entities, as they might find it difficult to identify if their customers have a nominee director or shareholder.

Option 2(b): Require reporting entities to obtain information from companies as to the existence of any nominee directors and shareholders and conduct ECDD if these relationships exist (preferred)

This would assist the reporting entity with determining whether the nominator has effective control of the company and is therefore a beneficial owner. It would also assist the reporting entity with determining the level of risk posed by the customer and the appropriate level of CDD that should be

¹⁵ See, for example, Discussion Document: Increasing the Transparency of the Beneficial Ownership of New Zealand Companies and Limited Partnerships, Ministry of Business, Innovations and Employment, June 2018.

conducted.

G.3 Stakeholders' views

We initially proposed to require enhanced CDD (ECDD) for legal persons with nominee directors to mitigate the misuse of nominee directors. The basis for this proposal is that companies with nominee shareholders or shares in bearer form are subject to ECDD. Nominee shareholders and shares in bearer form are another method of obscuring beneficial ownership and carry similar ML/TF risks to nominee directors, therefore companies with nominee directors should be subject to the same level of CDD.

Feedback from submitters was mixed. Five submitters supported the proposal at least in principle while three submitters opposed the proposal. The primary concern was how reporting entities would practically be expected to determine whether the legal person has a nominee director. This concern was also raised by submitters who supported the proposal in principle.

Upon further analysis of the risks posed by nominee directors and the points raised by submitters, we consider that the issue is with identifying companies that have nominee directors and shareholders rather than the level of CDD the companies are subject to. In particular, requiring ECDD on companies with nominee directors is unlikely to be effective if reporting entities are unable to identify those companies when establishing a business relationship.

We therefore instead recommend issuing a regulation that requires reporting entities to obtain information from companies as to the existence of any nominee directors and shareholders and the identity of the nominator. This would assist the reporting entity with determining whether the nominator has effective control of the company and is therefore a beneficial owner. It would also assist the reporting entity with determining the level of risk posed by the customer and the appropriate level of CDD that should be conducted. Finally, if a company refuses to provide this information the reporting entity will be prohibited from providing any relevant services to the company.

All other AML/CFT agencies support our preferred option.

G.4 Impact analysis			
	Option 1: status quo (no action taken)	Option 2: Require reporting entities to conduct ECDD on companies with nominee directors or shareholders	
		Option 2(a): Require companies with nominee directors to be subject to ECDD	Option 2(b): Require reporting entities to obtain information from companies as to the existence of any nominee directors and shareholders and the identity of the nominator (preferred)
Effectiveness at detecting and deterring ML/TF	0	<p style="text-align: center;">0</p> <p>The option has the potential to substantially address the vulnerability associated with companies with nominee directors. This, however, is undermined by the difficulty reporting entities will face in identifying the nominee directors as nominee directors are not recorded on the company register.</p>	<p style="text-align: center;">+</p> <p>This option also has the potential to substantially address the vulnerability associated with companies with nominee directors, as well as enhance the mitigation of the risks posed by companies with nominee shareholders. Requiring companies to provide this information as part of CDD will ensure that reporting entities will conduct ECDD when required.</p> <p>There is a risk that companies will not disclose information, however doing so requires the company to lie to the reporting entity, which can raise suspicion.</p> <p>Requiring companies to provide information about nominee directors and shareholders also allows for intelligence insights to be gathered as to the extent that New Zealand companies use these structures and arrangements.</p>
Proportionality	0	<p style="text-align: center;">+</p> <p>While this option will impose a degree of compliance burden on some reporting entities, we consider this degree of compliance burden justified by the high risk of ML/TF associated with companies with nominee directors.</p>	<p style="text-align: center;">+</p> <p>This option would impose a degree of compliance burden on some reporting entities, but we consider this justified by the vulnerability associated with companies with nominee directors.</p>
Practicality	0	<p style="text-align: center;">--</p> <p>Because this option does not address difficulty reporting entities may face in identifying the nominee directors, it is not easy for them to understand and implement.</p> <p>While this difficulty may be addressed throughs supervisory guidance, this may incur burden for the supervisors.</p>	<p style="text-align: center;">++</p> <p>We consider this a practical option in assisting the reporting entity with determining the level of risk posed by the customer and the appropriate level of CDD that should be conducted. If a company refuses to provide this information the reporting entity will be prohibited from providing any relevant services to the company.</p> <p>Also easy for supervisors to monitor as an ECDD is required.</p>
Overall	0	-	++

(H) Providing a limited exemption for court-appointed liquidators

H.1 What is the policy problem or opportunity?

A liquidator appointed by an order of the High Court under section 241(2)(c) of the Companies Act 1993 (court-appointed liquidator) will attract AML/CFT obligations and therefore be required to conduct CDD on their customer. Court-appointed liquidators were included in the AML/CFT regime through the AML/CFT Amendment Act 2017.

Court-appointed liquidators have faced two difficulties with complying with their AML/CFT obligations:

- first, court-appointed liquidators do not have an obvious customer upon which to conduct CDD. The appointment is made by the Court on the application of a creditor, and the company is forced into liquidation if the application is granted. Further, the liquidation is done for the benefit of the creditors of the company; and
- second, due to the nature of the appointment, the company may be unwilling or unable to provide the information required for CDD. If the company is the customer, the liquidator cannot proceed with the liquidation until CDD is completed. This directly conflicts with the obligations to conduct the liquidation under section 241(2)(c) of the Companies Act 1993.

H.2 What options have been considered?

Option 1: Status quo

This option means that no measure will be adopted to address the difficulties court-appointed liquidators face as identified above.

Option 2: Exempt court-appointed liquidators from some CDD requirements (preferred)

This option seeks to exempt court-appointed liquidators from some CDD requirements in respect of the company they have been appointed to liquidate. This option proposes to introduce a new regulation prescribing that the customer of a court-appointed liquidator is the company in liquidation. It would then provide a limited exemption for court-appointed liquidators from the following CDD requirements:

- standard CDD (section 14 — section 17 of the AML/CFT Act);
- enhanced CDD except for where enhanced CDD is required in situations of wire transfers and activities that require reporting entities to report suspicious activities (section 22(1), 22(2), 22(4), 22(5), 22(6), and 26 of the AML/CFT Act); and
- ongoing account monitoring (section 31 of the AML/CFT Act).

This means that this exemption would not apply when the liquidator pays out a creditor who is a beneficial owner or when making an international wire transfer to pay a creditor in a different jurisdiction. In these two situations, the liquidators would be required to conduct CDD to identify beneficial owner and obtain the information required for an international wire transfer.

H.3 Stakeholders' views

All submissions received were in support.

All other AML/CFT agencies support our preferred option.

H.4 Impact analysis		
	Option 1: status quo	Option 2: Exempt court-appointed liquidators from some CDD requirements (preferred)
Effectiveness at detecting and deterring ML/TF	0	<p style="text-align: center;">+</p> <p>This option enables court-appointed liquidators to conduct CDD (which currently is not feasible as discussed above) on higher-risk companies/services, therefore improves the effectiveness of the regime to detect and deter ML/TF.</p>
Proportionality	0	<p style="text-align: center;">+</p> <p>By providing a limited exemption from CDD, this option reduces the compliance burden of court-appointed liquidators, while ensuring that CDD is conducted for higher-risk customers and services.</p>
Practicality	0	<p style="text-align: center;">++</p> <p>This option addresses the issues around the difficulties of court-appointed liquidators' compliance with CDD requirements, making it easy for court-appointed liquidators to understand the scope of their obligations and compliance.</p>
Overall	0	<p style="text-align: center;">++</p>

(I) Allowing for a risk-based approach to be taken for section 59 audits

I.1 What is the policy problem or opportunity?

The AML/CFT Act currently requires reporting entities to ensure that its risk assessment and AML/CFT programme are audited every two years. The relevant AML/CFT Supervisor can also request an audit be conducted at any time.

The minimum audit period of every two years does not provide much flexibility for supervisors to apply a risk-based approach with respect to requiring reporting entities to conduct audits. For example, it may be consistent with a reporting entity's ML/TF risk to require an audit every three or four years; however, this is not possible with the current timeframes prescribed in the Act.

Reporting entities may demonstrate that they are low-risk by, for example, providing products or services with low money laundering or terrorism financing risk or supervisory inspections showing consistently high levels of compliance. In those instances, a less frequent audit may be more appropriate.

I.2 What options have been considered?

Option 1: Status quo

No action would be taken.

Option 2: Set a maximum of three years between audits

This option sets the maximum timeframe for audits to every three years and relies on supervisors to require more frequent audits for higher-risk entities.

Option 3: Set a maximum of four years between audits

This option sets the maximum timeframe for audits to every four years. Similar to option 2, it also relies on supervisors to require more frequent audits for higher-risk entities.

Option 4: Set a maximum of three years with an additional option of four years for reporting entities the relevant supervisor identifies as "low-risk" (preferred)

Option 4 is a hybrid of option 2 and 3. It would set the appropriate default timeframe for most reporting entities and therefore minimise the operational burden on the supervisors as compared to option 3. Compared to Option 2, this option also allows for a longer timeframe for entities the supervisor determines to be "low-risk" due to the nature of the services the entity provides as well as their compliance history.

I.3 Stakeholders' views

RBNZ and DIA indicated preference for option 4 over option 2 and 3. FMA prefers the status quo (2 years) but is comfortable with option 4.

Almost all submissions were in support of the proposal of a longer timeframe between audits. Two opposed the proposal on the basis that a longer timeframe may increase the cost of the audit due to a longer timeframe being under examination.

While we agree with these two submitters that a longer timeframe between audits may increase the workload required to conduct the audit and the potential for remediation work following, we consider that this issue is outweighed by the general benefit of reducing demand on the audit market and

allowing for a more flexible approach. In practice, those entities that receive audits on longer timeframes are those that have demonstrated their low ML/TF risk nature.

We also asked submitters to indicate their preference as to the appropriate timeframe between audits. Five submitters supported a three-year timeframe while six submitters supported a four-year timeframe.

I.4 Impact analysis				
	Option 1: status quo	Option 2: maximum timeframe 3 years	Option 3: maximum timeframe 4 years	Option 4: maximum 3 years, but allow for 4-year timeframe for low-risk entities (preferred)
Effectiveness at detecting and deterring ML/TF	0	0 Approximately the same amount of impact on detecting or deterring ML/TF as supervisors would still be able to request an earlier audit.	0 Approximately the same amount of impact on detecting or deterring ML/TF as supervisors would still be able to request an earlier audit.	0 Approximately the same amount of impact on detecting or deterring ML/TF as supervisors would still be able to request an earlier audit.
Proportionality	0	+ A longer timeframe may require the supervisors to request more audits at an earlier stage, which may cause a degree of operational burden on the supervisors. However, a longer timeframe reduces the compliance burden for reporting entities to a significant degree that is consistent with the ML/TF risk associated with the majority of the reporting entities.	0 This would impose a significant amount of operational burden on supervisors, as they would need to require an earlier audit for most reporting entities who are of low ML/TF risk (and therefore a three-yearly audit timeframe is more appropriate). Because the majority of reporting entities would be required to conduct a three-yearly audit, and a small number of low-risk reporting entities would be required to conduct a four-yearly audit, this option would reduce the compliance burden for those reporting entities. This effect, however, is negated by the operational burden on supervisors. We therefore consider the impact to be overall neutral.	++ This option aligns the compliance burden of most reporting entities to a degree that is proportionate to their ML/TF risk, as the majority of them are of medium-risk, and therefore a three-yearly audit is more appropriate. While this proposal is expected to incur additional costs for AML/CFT Supervisors as they would need to request more frequent audits from higher-risk reporting entities if required; and requesting less frequent audits from lower-risk reporting entities, if required. This slight increase in costs to supervisors (see table 5.2) is more than offset by the reduction in compliance burden and costs to reporting entities.
Practicality	0	0 This option is unlikely to require substantial additional effort to implement as a three-year audit is appropriate for most reporting entities.	- Because supervisors would need to prescribe more frequent audits for the majority of reporting entities, this option would be more difficult to implement compared to the status quo.	0 As with Option 2, this option is unlikely to require substantial additional effort to implement.
Overall	0	+	-	+

Section 4: Conclusions

5.1 What option, or combination of options, is likely best to address the problem, meet the policy objectives and deliver the highest net benefits?

Overall, the Ministry of Justice recommends the following approaches to the eight issues we have identified with the two sets of expiring Regulations. The issues listed below are independent of each other and therefore decisions can be taken separately. All proposals require amendments to the Definitions Regulations and Exemptions Regulations.

- A. reissue Regulations with necessary changes so that the regulations remain fit for purpose and in line with the risk environment;
- B. amend Regulation 24A of the Definitions Regulations to prescribe that customer due diligence must be conducted before an offer to lease is presented to the lessor for commercial lease transactions;
- C. amend Regulation 16 of the Exemptions Regulations to include within the scope of the regulation entities that are in partnership as well as entities where A is 'controlled' by B (and vice versa) or where A and B are both controlled by C; and define "control";
- D. issue a regulation prescribing that related limited partnerships established under the Limited Partnerships Act 2008 are eligible for inclusion in a designated business group;
- E. issue a regulation exempting from the scope of 'managing client funds' money paid to a reporting entity for the purposes of the reporting entity paying a third party where that third party is:
 - a New Zealand Government department, New Zealand Police, or local authority; or
 - a barrister, expert witness, and professional mediator and adjudicators carrying out its business in New Zealand; or
 - any other third party carrying out its business in New Zealand where the value of the transaction, or series of transactions, is less than \$1,000.
- F. issue a regulation exempting reporting entities subject to a section 143(1)(a) order or a production order from all requirements to conduct enhanced customer due diligence with respect to the customer that is the subject of the order for a period of 30 days unless otherwise notified by the Police;
- G. issue a regulation requiring reporting entities to obtain from a customer that is a company information as to whether any of its directors or shareholders are nominee directors or shareholders and, if so, conduct ECDD of these customers;
- H. prescribe that a customer of a liquidator appointed by an order made under section 241(2)(c) Companies Act 1993 (court-appointed liquidators) is the company in liquidation; and also exempt court-appointed liquidators from all requirements to conduct customer due diligence except where:
 - the liquidator is paying a beneficial owner of the company in liquidation, in which case the liquidator must conduct customer due diligence before paying the beneficial owner according to the level of risk involved; or
 - the liquidator is making a wire transfer; and
- I. prescribe that audits must be completed every three years, or, if the relevant AML/CFT Supervisor determines the entity to be low risk, four years.

5.2 Summary table of costs and benefits of the preferred approach

Affected parties	Comment	Impact	Evidence certainty
Additional costs of proposed approach, compared to taking no action			
AML/CFT reporting entities	Proposal G Requiring reporting entities to ascertain from their customers whether any of its directors or shareholders are nominee directors and shareholders, and if so, conducting ECCD on them is likely to incur additional ongoing compliance costs for some reporting entities.	Low Although it is impossible to ascertain the number of companies that have nominee directors, as it is unattainable to scope the number of companies this proposed regulation would have an impact on, we do not expect this to be overly onerous as companies are <i>de facto</i> required to hold information about the beneficial ownership (including the existence of nominee directors or shareholders) in order to comply with a Registrar’s request under sections 365A — 365H of the AML/CFT Act.	Low-Medium
AML/CFT Supervisors: DIA, FMA and RBNZ	Proposal D is expected to incur additional costs on AML/CFT Supervisors to process applications to form a DBG from related limited partnerships	DIA: \$10,000 maximum for staff time, one-off cost FMA: \$10,000 a year maximum in staff time RBNZ: Negligible	Medium-High
	Proposal I is expected to incur additional costs for AML/CFT supervisors as they would need to request more frequent audits from higher-risk reporting entities if required; and requesting less frequent audits from lower-risk reporting entities, if required.	DIA: \$1,000 one-off cost, and \$5,000 a year in staff time as on-going cost FMA: \$10,000 a year maximum RBNZ: Negligible	Medium-High
Police	Proposal F is expected to incur costs for Police as it would be required to monitor entities subject to Commissioner’s orders and production orders to determine whether an	Nominal	Medium-High

	extension of the exemption is required		
Reporting entities' customers	Flow-on impacts from Proposal G	Very low	Low
The general public	Flow-on impacts from Proposal G	Negligible	Medium-High
Total Monetised Cost			
Non-monetised costs		<i>Low</i>	Low-Medium

Expected benefits of proposed approach, compared to taking no action			
Affected parties	Comment	Impact	Evidence certainty
AML/CFT reporting entities	Our proposals B, C, D, E, H, I are expected to ensure the compliance burden for reporting entities and transactions is proportionate to their ML/TF risk, particularly where the entities/transactions are low risk.	High	Low-Medium
Reporting entities' customers	Flow-on benefits from the compliance burden for reporting entities being reduced	Low	Low
The wider government	Our proposals F and G are expected to address areas of ML/TF vulnerability by reducing the potential for criminals to misuse nominee director or nominee shareholder arrangements, and by avoiding tipping off customers that are subject to an inquiry. It would also contribute to maintaining and enhancing New Zealand's international reputation, and give better effect to the AML/CFT regime's risk-based approach by prescribing audit timeframes that better reflect	Medium	Medium

	the reporting entities' ML/TF risk.		
The general public	Our proposals F and G are expected to prevent the general public from being misused by criminals, which would contribute to public confidence in the financial system.	Medium	Medium-High
Total Monetised Benefit			
Non-monetised benefits		<i>Medium-High</i>	Medium

5.3 What other impacts is this approach likely to have?

The significant diversity in businesses that have AML/CFT obligations is an inherent challenge for the AML/CFT regime as it can be difficult to ensure that a regulation functions appropriately for every type of captured business. For example, a proposal may function correctly for a bank, but may not function correctly for a real estate agent.

Owing to the nature of the proposals, the impact of this challenge is unlikely to be significant (as no significant changes are proposed). Nevertheless, we have minimised this by consulting with a diverse range of industry stakeholders and peak bodies. In addition, we have ensured that, where possible, proposed changes are not linked to a type of business or business structure. If the impact of this challenge eventuates, it can be mitigated through Ministerial exemptions¹⁶ and the statutory review of the AML/CFT Act scheduled in 2021.

5.4 Is the preferred option compatible with the Government's 'Expectations for the design of regulatory systems'?

The preferred options are generally compatible with the Government's "Expectations for the design of regulatory systems".

Although there is currently no system stewardship approach to this regulatory area, the statutory review of the AML/CFT Act will necessarily include a review of the AML/CFT regulations. Additionally, the National AML/CFT Strategy agreed to by Cabinet [DEV-19-MIN-0270 refers] includes actions for the government to improve private sector engagement with the operation and governance of the regime. This will improve the AML/CFT regulatory regime's compatibility with the government's "Expectations for the design of regulatory systems".

¹⁶ Under section 157 of the AML/CFT Act, the Minister may exempt a reporting entity, a class of reporting entities, a transaction or a class of transactions from the requirements of all, or any of the provisions of the Act.

Section 5: Implementation and operation

6.1 How will the new arrangements work in practice?

The preferred options can be given effect by amendments to Exemptions Regulations, Definitions Regulations, and Cross-border Transportation of Cash) Regulations.

Ongoing Operation

The Ministry of Justice will administer these new regulations.

The AML/CFT Act established the AML/CFT co-ordination committee more commonly known as the National Co-ordination Committee (NCC) to ensure the consistent, effective, and efficient operation of the regime.

The NCC comprises of a representative from each of: the Ministry of Justice, Customers, AML/CFT Supervisors, Police and any other government agency employee as invited by (the chief executive of) the Ministry of Justice.

Enforcement

The AML/CFT Supervisors (DIA, FMA and RBNZ) will be responsible for the enforcement of the new arrangements by using regulatory tools that promote compliance by punishing non-compliance including formal warnings, performance injunctions, restraining injunctions and enforceable undertakings.

Additionally, the AML/CFT Supervisors are also responsible for educating and supporting reporting entities to comply with their AML/CFT obligations (eg, by providing guidance).

6.2 What are the implementation risks?

For proposal F “providing a limited exemption for reporting entities subject to a Commissioner’s Order or a production order”, some submitters have raised implementation concerns, such as who is responsible for monitoring the expiry of the order.

To ensure the practicability of this option, the supervisors and the Police will work together to develop guidance to support this exemption and address the practical questions raised by submitters during the targeted consultation.

Section 6: Monitoring, evaluation and review

7.1 How will the impact of the new arrangements be monitored?

The Ministry of Justice will monitor the effectiveness of these proposals.

The impact of the new arrangements will be monitored as part of the statutory review of the whole AML/CFT regime in 2021. All the AML/CFT regulations will be reviewed as part of this statutory review.

The National AML/CFT Strategy (Strategy) agreed to by Cabinet [DEV-19-MIN-0270 refers] includes actions for the government to improve private sector engagement with the operation and governance of the regime. This will improve the AML/CFT regulatory regime's compatibility with the government's "Expectations for the design of regulatory systems".

7.2 When and how will the new arrangements be reviewed?

As discussed above, the review of the AML/CFT regime is planned to take place in 2021 following the FATF mutual evaluation. This involves the review of the new arrangements.

A FATF mutual evaluation is when the FATF conducts peer-reviews of each member on an on-going basis to assess levels of implementation of the FATF recommendations. It involves the testing of a country's anti-money laundering and counter terrorist financing compliance regime against 40 key principles that FATF have determined are essential to combating these threats.

With New Zealand currently being assessed under the mutual evaluation, we anticipate the FATF will make recommendations on how to strengthen New Zealand's AML/CFT regime. These recommendations will be considered as part of the AML/CFT regime's statutory review in 2021, where the Ministry of Justice will be required by section 156A of the AML/CFT Act to review the operation of the provisions of the AML/CFT Act and consider whether any amendments to the AML/CFT Act are necessary or desirable.

The Strategy agreed by the Government will set the strategic direction for the AML/CFT regime. The Strategy will coordinate efforts across government and the private sector and guide prioritisation of work to improve the regime. This should provide more opportunities for stakeholders to raise concerns and to assess the proposed amendments.

Appendix 1 – Technical changes and revocations

Regulation	Change proposed
Definitions regulation 13A — <i>Inclusion: wire transfer of more than \$1,000</i>	Clarify that this regulation applies to ordering institutions for wire transfers that occur outside of a business relationship with a customer, as well as applying to beneficiary institutions for wire transfers that are received outside of a business relationship with a customer.
Definitions regulation 15 — <i>Inclusion: transactions involving certain stored value instruments</i>	Amend the definition of 'debit card' to replace the reference to 'financial institution' with 'bank and non-bank deposit taker'; ensure structuring with stored value instruments cannot occur.
Definitions regulation 16 — <i>Inclusion: certain financial advisors</i>	Update regulation to continue including financial advisors who are proximate to products and services offered by other reporting entities that carry a higher money laundering or terrorism financing risk, but without relying on the 'category 1' distinction.
Definitions regulation 18A — <i>Exclusion: non-finance businesses that transfer money to facilitate purchase of goods and services</i>	Clarify that the regulation does not apply to designated non-financial businesses and professions in respect of managing client funds; amalgamate this regulation with Exemptions regulation 13.
Definitions regulation 20 — <i>Exclusion: lawyers, etc</i>	Update heading to reflect amended scope of exemption (estate administration and family trusts); restructure the regulation to exclude the relevant activities instead of reporting entities who only provides the relevant activities.
Definitions regulation 21B — <i>Exclusion: persons carrying out property management activities</i>	Restructure the regulation to exclude the activity of property management from the scope of 'managing client funds' instead of excluding reporting entities which only provide that activity.
Definitions regulation 25 — <i>Financial Service Providers (Registration and Dispute Resolution) (FSPR) Act 2008 prescribed for certain purposes</i>	This regulation can be revoked as it is no longer required. This regulation prescribed the FSPR Act 2008 for information sharing purposes under section 140(2)(x), and the Statutes Amendment Act 2019 inserted the FSPR Act 2008 as section 140(2)(ha).
Exemptions regulation 8 — <i>Transactions that are not occasional transactions or wire transfers exempt from section 49(2)(d) of Act</i>	Clarify this regulation by repealing regulation 8(1)(b); repeal regulation 8(3) as it is unnecessary.
Exemptions regulation 11 — <i>Relevant services provided in respect of insurance policies that are closed to new customers and new premiums</i>	Clarify that the regulation only applies to life insurers and not all insurance policies.
Exemptions regulation 15 — <i>Relevant services provided in respect of certain stored value instruments</i>	Amend the definition of 'debit card' to replace the reference to 'financial institution' with 'bank and non-bank deposit taker'; ensure structuring with stored value instruments cannot occur.

<p>Exemptions regulation 17 — <i>Relevant services provided under premium funding agreement by insurance company</i></p> <p>Exemptions regulation 18 — <i>Relevant services provided under premium funding agreement by non-insurance company</i></p>	<p>The definitions for both reg 17 and reg 18 are contained within reg 17, which has the potential for confusion. As the regulations are similar in scope it is appropriate to amalgamate the regulations.</p>
<p>Exemptions regulation 19 — <i>Relevant services provided in respect of certain low-value life insurance policies</i></p>	<p>Remove contracts of consumer credit from scope of the regulation as they are pure risk contracts and exempt by virtue of Exemptions reg 12.</p>
<p>Exemptions regulation 20 — <i>Relevant services provided in respect of certain superannuation schemes</i></p> <p>Exemptions regulation 20A — <i>Relevant services provided in respect of certain employer superannuation schemes</i></p>	<p>Update these regulations to also capture retirement schemes excluded by the 'Services provided in relation to certain retirement schemes' exemption. This class exemption was intended to act as a temporary solution as some retirement schemes cannot rely on reg 20A.</p>