New Zealand Law Society
Te Kāhui Ture o Aotearoa

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AML/CFT Act Consultation Team
Ministry of Justice

By email: aml@justice.govt.nz

Re: AML/CFT Regulations – exposure draft

1. The New Zealand Law Society Te Kāhui Ture o Aotearoa welcomes the opportunity to comment on the exposure draft of the proposed changes to regulations made under the Anti-Money Laundering and Countering Financing of Terrorism Act (AML/CFT Act).

2. This submission refers to both the exposure draft regulations, and the accompanying consultation document. The Law Society's comments are limited to those substantive aspects relevant to the legal profession.

General comments

3. The approach taken in the draft amendments generally reflects the Ministry's intention to make regulatory amendments which seek to give relief to businesses and to respond to immediate issues identified by the statutory review which took place between July 2021 and June 2022. The Law Society supports this approach in the context of the AML/CFT Act, and the risk-based regime created by that Act.

4. As the Law Society set out in its submission on the 2021 statutory review,[1] it is hoped that the Ministry will address the main issue identified by lawyers, that is, that there are identified areas where the time and cost required by lawyers to comply with their AML/CFT obligations is disproportionate to the actual risk of money laundering and terrorism financing posed by their business activities, and sometimes duplicate existing professional requirements.

5. The Law Society notes that in some instances, the proposed amendments appear to create additional requirements for lawyers. However, we recognise the intent of the amendments is generally aimed at providing the clarification sought by lawyers as to what their obligations are, and when those obligations are triggered.

6. By way of example, it remains unclear whether the exceptions allowing for sharing of a compliance officer and sharing CDD information within designated business groups provide any relief or practical assistance to lawyers, given the structure of legal practice in New Zealand. Under the Lawyers and Conveyancers Act 2006 (**LCA**) a lawyer or an incorporated law firm is prohibited from sharing income from any business involving the provision of regulated services to the public with any person who is not a lawyer or an incorporated law firm. This restriction includes overseas law firms. There are also restrictions upon who may be a director or shareholder of an incorporated law firm. Some lawyers and law firms do form networks to share resources and marketing costs, but they are each independently owned and controlled. It is difficult to see how law firms could be "related" as required by paragraph (d)(vi) of the definition of designated non-financial business or profession in section 5 of the AML/CFT Act.

[1] https://www.lawsociety.org.nz/assets/Law-Reform-Submissions/I-MOJ-AMLCFT-Review-10-12-21.pdf

It is therefore unclear whether the proposed amendment is intended to be of assistance to the legal profession. If proposed regulations 14, 18 and 38 are intended to assist lawyers, then issues such as the effect of regulation 14 on existing elections should be made clear.

7. As to the clarity of the proposed amendments, the Law Society appreciates that without legislative reform to the AML/CFT Act itself, the ability to tackle some of the issues by regulation is somewhat restricted. However, the number of different regulations and the necessary cross referencing between them and sections of the Act, naturally hinders clarity. To that end, we have made only limited drafting suggestions.

8. The extended timeframes for filing suspicious activity reports and prescribed transaction reports are helpful and more realistic for lawyers.

Proposed amendments to the Anti-Money Laundering and Countering Financing of Terrorism (Requirements and Compliance) Regulations 2011

Regulation 11A – Additional information required for standard CDD on legal persons and legal arrangements

9. New regulation 11A(2)(d) will require reporting agencies to obtain information about the settlors and protectors of trusts, specifically the name and date of birth of those individuals. The Consultation Document acknowledges this information can be difficult to obtain and/or verify, and queries whether regulations should provide guidance on what a reporting entity should do in circumstances where CDD cannot be completed.

10. The Law Society agrees that completion of CDD for settlors and protectors can be challenging, in particular where – as the Consultation Document notes – a settlor is deceased. Further, settlors and protectors may not be captured as a beneficial owner. In these instances, this is results in over compliance.

11. The Law Society considers this risk is adequately met by the CDD requirements for those captured by the definition of beneficial ownership under section 5 of the Act, and any further guidance is best issued by the relevant supervisors. The Law Society recommends regulation 11A(2)(d) be removed.

Regulation 12A – When simplified CDD does not apply

12. The intention of new regulation 12A is to declare that simplified CDD is not appropriate where there may be grounds to report suspicious activity. However, it is drafted in the negative and is therefore less clear than it otherwise could be. A reporting identity could interpret this as suggesting they are not required to undertake CDD at all. The Law Society recommends that the new regulation should clearly specify what level of CDD *is* required, e.g. standard or enhanced.

13. This could be achieved with drafting such as: '*Despite section 18(1) and (3) of the Act, a reporting entity must conduct enhanced customer due diligence on a person in the circumstances described…'.*

Regulation 12C – Enhanced CDD and trusts

14. The Consultation Document asks whether the Regulations should define a 'low risk' trust. The Law Society supports the introduction of this concept, and considers that providing for trusts that are, for example, small, or long-established, and where the settlors are known to, and the activities or proposed activities (i.e. purpose(s) of the business relationship) of the trust are well understood by, the lawyer concerned should ensure that situations that involve a low money laundering and terrorism financing risk would require a reduced level of CDD. This

would be consistent with the purposes set out in section 3 of the AML/CFT Act, reduce unnecessary costs, and improve consistency across reporting entities applying this exemption.

15. The Law Society proposes, as a practical way to deal with this issue, that (with one exception, discussed below) a precise statutory definition of what constitutes a "low-risk trust" in respect of which a reporting entity is not required to verify information relating to the source of funds or source of wealth would be inconsistent with the risk-based approach. Instead, the Law Society considers it would be preferable to allow a reporting entity to designate a trust as "low risk" on reasonable grounds (possibly following guidance issued by statutory supervisors). This could also be supported by a requirement for senior management approval (as in the cases of PEPs and correspondent banking relationships) and the requirement to keep records of the grounds upon which the trust was designated low risk. Consultation on supervisor guidance around low-risk trusts would be appreciated before this guidance is published.

16. It would also be of assistance if trusts, the settlor or settlors of which are deceased, could be designated low-risk trusts in all circumstances (unless the reporting entity considers the level of risk involved is such that enhanced due diligence should apply to a particular situation). This is because the death of a person is unlikely to form part of an ML/TF offence, and the difficulties in verifying (as opposed to enquiring about) source of funds or source of wealth where that source is a deceased person can create significant difficulties that are disproportionate to the level of ML/TF risk, particularly with lapse of time (which may be significant, bearing in mind that private trusts can last up to 125 years under New Zealand law).

Regulation 12D – Additional enhanced CDD

17. The Consultation Document explains that proposed new regulation 12D is intended to require implementation of one or more of the additional enhanced CDD measures only if and where it is necessary to do so to effectively mitigate the risk of money laundering and financing of terrorism.

18. As drafted, regulation 12D sets out clearly what the additional enhanced customer due diligence measures are. However, it requires an assessment of when they are 'necessary.' A possible unintended consequence is that different reporting entities will interpret "as is necessary" differently. This could lead to compliance uncertainty, and customers preferring some reporting entities over others because the entities are known for tending to not carry out additional enhanced CDD measures.

19. We note that regulation 12C regarding when enhanced CDD is not required is incomplete. It may be this is intended to clarify the term 'necessary'.

Proposed amendments to the Anti Money Laundering and Countering Financing of Terrorism (Definitions) Regulations 2011

Regulation 7B – Managing client funds, 'fees for professional services'

20. The Law Society considers that the proposed definition is inconsistent with a risk-based approach in that it is too restrictive and does not reflect the reality of business practice. The Law Society's view is that the definition of "fees for professional services" in the context of law firms should explicitly extend to amounts ordinarily incurred and disbursed incidentally in the course of acting for a client and which pose low, or no, risk of ML/TF – such as Court, LINZ (registration and OIO costs) and other government/local government agency/department filing fees (such as for the IRD binding ruling applications and the costs of licence applications), process servers, translators' fees, fees for expert witnesses in proceedings and similar.

Regulation 7C – Engaging in or giving instructions on behalf of customer to another person

21. The proposed regulations provide that for the purposes of subparagraph (a)(vi) of the definition of designated non-financial business or profession in section 5(1) of the Act, engaging in or giving instructions on behalf of a customer to another person means any action taken by the person to whom that subparagraph applies on behalf of the customer in preparing for, or giving instructions relating to, a transaction or transfer in circumstances where the activities in subparagraph (a)(i) to (v) of that definition are not carried out.

22. The Law Society considers this provision may be ultra vires, at least insofar as it purports to apply to lawyers. This is because section 6(4)(c) provides that "*in the case of a law firm, conveyancer, incorporated conveyancing firm, accounting practice, real estate agent, or other designated non-financial business or profession, the activities carried out by that reporting entity are activities described in the definition of designated non-financial business or profession in section 5(1)".* Section 5(1)(a)(vi) is not engaged unless "*a law firm, a conveyancing practitioner, an incorporated conveyancing firm, an accounting practice, a real estate agent, or a trust and company service provider, who, in the ordinary course of business, carries out"* the relevant activity. Paragraph (b) of the definition can include a person or class of persons in the definition, but does not allow for an activity (or, as in this case preparatory work or related instructions) to be brought within the definition. Such an approach would introduce confusion in relation to other provisions of the AML/CFT Act as well, including the section 39A (definition of suspicious activity).

Regulation 13B – Wire transfers made by DNFBP of $1,000 or more through another reporting entity

23. While new regulation 15B provides relief to DNFBPs of the wire transfer provisions under sections 27 and 28 of the principal Act, this could be improved by a further small amendment in line with some of the medium to long-term intended relief in recommendations arising from the Statutory Review,[2] and consistent with a risk-based approach.

24. As DNFBP's remain obligated to file PTR's and there is little risk associated with domestic transfers, it makes sense to restrict application of new regulation 13B to international wire transfers (IWTs) or in other words, part (a) of the prescribed transaction definition in the Act.

25. IWT's contain greater risk than domestic transfers:

    a. IWT's cannot be as efficiently traced as a domestic transfer.

    b. Where CDD is required, a NZ non-client's reporting entity should hold this information, whereas an offshore reporting entity may not be as reliable.

26. The Law Society therefore recommends a small amendment to new Regulation 13B, to change the word "wire transfer" to "international wire transfer". This would provide immediate relief to DNFBPs and is consistent with DNFBP IWT prescribed transaction reporting requirements.

Proposed revocation of exemptions regulation 24

27. The Law Society has concerns about the effects of this proposed revocation, in terms of the increased costs imposed on business, without reducing ML/TF risk.

28. The proposed revocation appears to be considered appropriate because of other changes to the beneficial owner definition and a change to the ownership threshold. The practical effect

[2] Recommendations 141, 143, and 737.

though is to remove the ability for one reporting entity (A) to rely on a customer (B) being a reporting entity and simply being able to obtain the relevant information if required. This can be helpful for law firm reporting entities with reporting entity clients. The proposed revocation appears to stem from concerns about the transparency of trusts and the ability to identify the beneficial owners of trusts generally expressed in the review and is an apparent misunderstanding of what a "trust account" is, and how it operates in practice.

Ngā mihi nui

David Campbell
Vice President