

AML/CFT review begins to tackle major issues

Geoff Adlam - Wed, 3 May 2023

- **International Financial Action Taskforce**
- **International Bar Association**
- **anti-money laundering and countering financing of terrorism**
- **Anti-Money Laundering and Countering Financing of Terrorism Act 2009**
- **regulations**
- **Ministry of Justice**
- **Department of Internal Affairs**

Consultation on proposed amendments to significant regulations under the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 closed in April, with some changes potentially in force by July.

But resolution of “many more chunky issues” could take several years, Auckland barrister and AML/CFT expert Gary Hughes says.

The consultation by the Ministry of Justice followed its major review of the Act which was tabled in Parliament on 7 November 2022. This statutory review itself followed the international Financial Action Task Force evaluation of New Zealand’s anti-financial crime regime in 2021.

Hughes is Chair of the International Bar Association’s AML & Sanctions Experts committee, and a member of the Ministry’s expert industry advisory group on this review process. *Capital Letter* interviewed him in the wake of his newsletter to clients on the consultation.

Recapping the Ministry’s review paper in late 2022, he says it ended up concluding New Zealand is “fit for purpose - well, only just barely”.

The Ministry found the country has a generally sound regulatory regime which provides a solid basis to detect and deter money laundering or terrorism financing.

However, problems exist that prevent the regime from being ‘the best it can be for New Zealand’. In particular, the review felt New Zealand should be following a more risk-based approach, instead of having overly prescriptive requirements. Hughes feels that “many law firms can probably relate to that”, after experiencing five years of the Department of Internal Affairs’ “prescriptive requirements”.

The Ministry would like to see more tailored guidance to be provided to firms. Currently, some aspects of AML law require all businesses to comply to the same one-size-fits-all standard regardless of their size or risk profile, which Hughes agrees ends up “largely ignoring the FATF’s endorsement of a risk-based proportionate approach allowing an element of discretion.”

He says the proposed regulatory changes start the first of a three-phase review process by “filtering out from 215 recommendations a first package of ‘early’ law changes - with a multiplicity of changes to existing regulations, and adding new ones”.

This current short-term package is for issues where the review was able to make a clear or generally agreed recommendation for what change is needed and how.

“These things can be implemented (or squashed into shape) by new or amended regulations, bypassing the need to go back to Parliament. For example, we are trying hard to obtain some regulatory relief for low-risk trusts, although there are many different opinions around how the Ministry might delineate what types of trust are genuinely less risk, without opening up a loophole that others may exploit.”

Some difficult aspects to be reconsidered in the next phase

However, Hughes says, other important aspects of New Zealand’s whole financial crime framework are up for reconsideration during this review, including matters which the FATF and international community are “urging us to take up or improve”.

"For instance, the 2021 Mutual Evaluation identified New Zealand’s rather underdeveloped regime and lack of regulator for dealing with international Targeted Financial Sanctions. While MFAT has grown at pace since then, in response to country-specific sanctions against Russia and Belarus, more development is needed.

“Then there are other new areas probably even more remote to Kiwis, such as nuclear Proliferation Financing rules aiming to slow the spread of weapons of mass destruction. How the Ministry will make that pragmatic and right-sized for NZ conditions remains a guessing game”.

He noted phase 2 of the review also enables us to go back to the drawing board on “foundational assumptions in the AML regime, such as whether it is desirable to persist with three separate Supervisors (the DIA, FMA, and RBNZ) – as well as the Moj, NZ Police Financial Intelligence Unit, NZ Customs and/or Inland Revenue all having a role to play.”

Timing problems

Hughes says there will be many important topics yet to flow in the medium term and long-term packages of outcomes still to be released. There remains uncertainty of timing, making it hard for private sector reporting entities to gear up and plan for participation at the right time.

“Additionally, New Zealand is in the middle of an election year cycle, so finding time for Cabinet to actually approve further changes this term will be tricky.”

Hughes says after the current short-term package, a range of medium-term issues might be tackled through operational changes (such as better, more tailored guidance) or other potential regulatory changes to be debated because thus far “no clear consensus emerged on what recommendation the review should make”. An example of that might be “whether and to what extent the open market for AML Auditors needs to be licensed or quality-controlled in some way”.

He says most will require further policy work and private sector consultation before the next set of draft Regulations can be prepared. At this stage he sees the best hope as release of a medium-term package later in 2023 but notes “this is perhaps at risk of not emerging before the election”.

Long-term changes

The third phase is long-term changes which will require Parliament to amend the AML/CFT Act.

“Some of these changes might be widely agreed already, or technically straightforward, but some potentially go to the core of the AML/CFT regime we’ve had in place since 2009. The crush on finding Parliamentary legislative time is such that apparently even getting a new bill introduced into the House by the end of 2024 would be ambitious. Then getting it passed before end of 2025 could be the aim – although by then it may become stuck in a political lottery again with the next electoral cycle!”

Added complexity

Hughes says it is encouraging how well the Ministry is engaging in consultation and listening to input. He sees the phase one regulatory fix involving 80 new and amended regulations as making “some welcome improvement in compliance issues and definitions that have seen variable levels of compliance amongst reporting entities – such as Ultimate Beneficial Owners and what exactly must be done if placing Reliance on Third Parties to carry out your CDD”.

Just under half the current proposed Regulation changes are expected to be in force by 31 July while the rest - some 46 or so separate amendments - are delayed and will come into effect on 1 June 2024.

However, one result of the short-term regulatory initiative may be added complexity in the law.

"With so many details now changing in regulations (which are subsidiary legislative documents) and adding to a legal obligation, or in some cases even altering the meaning of the AML/CFT Act itself, the overall regime will become more complex and more layered. Finding an answer to a compliance question will now hardly ever be available by resorting to the Act alone."

Hughes says many nuances and extra steps will pop up in the regulations instead, and reporting entities will need to pay close attention in re-training staff and re-writing programmes.

"Officials genuinely want to improve the messy, complex AML/CFT regime. But there is a lot of improvement still to be had."

Australian lawyers soon to gear up for AML too?

Finally, Hughes noted recent moves by the Australian Attorney-General's Office to finally begin implementation of AML coverage for lawyers, accountants, and real estate dealers there too. A consultation paper on modernising and simplifying Australia's anti-money laundering and counter-terrorism financing regime is open for submissions until mid-June.

"Known as 'tranche two' over there, our Aussie friends have been dragging the chain on this for years but are coming under increasing international pressure to commit, as the FATF is due to visit and evaluate their AML regime at end of next year."

If that proceeds, Hughes says in some ways it "should assist New Zealand lawyers who end up dealing with Australian firms that are unregulated for AML, and often mystified by notions of client due diligence or KYC." However, he adds "I really hope they take the opportunity to simplify their system first, as the discussion paper suggests. That remains what is largely missing in the New Zealand scene too."

Lawyers interested in seeing a copy of Hughes' full client newsletter can email gary@garyhughes.nz.