



30 September 2009

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Dear Ben

Anti-Money Laundering and Countering Financing of Terrorism Reform – Background Information Document

Investment Savings and Insurance Association (“ISI”) has provided a submission to the Foreign Affairs and Defence Select Committee on the Anti-Money Laundering and Countering Financing of Terrorism Bill and has also, at the request of the Committee, provided a supplementary submission on reasons for a more risk-based approach.

ISI has participated in consultation with the Ministry of Justice on AML/CFT since at least 2005 and we look forward to the opportunity to be involved in further consultation following enactment of the Bill as the regulations, codes of practice and guidelines are developed.

We have made only general comments on the Background Information Document, in the expectation that most points covered would form part of the consultation process to come. We have no objection to the release of these comments and we would be more than happy to discuss them if that would be useful.

We note that the Bill has now been reported back from the Select Committee and we endorse the changes made by the Committee in respect of:

- A more risk-based approach
- Greater harmonisation with Australia

- Limitation of the scope of PEPs

We are disappointed that a definition of life insurance has not been included in the reported back Bill as we believe a definition is necessary to clarify the effect of paragraph (a)(xii) of the definition of financial institution. While we believe the intention is that pure risk insurance is not to be covered by the Bill we recommend that the drafting of the regulations should include a clarification or a specific exemption for that class of product.

We recommend that the following points should be included in consultation on the development of regulations and guidelines.

Comments on Document

Customer Due Diligence

The ambiguity in paragraph (a) (xii) of the definition of financial institution has not been remedied in the reported back Bill. Consequently the regulations will need to clarify exactly what is intended by ‘underwriting’ and by ‘life insurance’ in that context. The nature of the life insurance contract, the underwriting process (where, in particular, an insurer applies ‘reasonableness’ criteria on the amount of insurance provided depending on the insured’s personal circumstances) and that the premium is a relatively small annual amount set by the insurer, means that life insurance, including traditional whole of life and endowment policies, provide a low risk of money laundering.

We endorse the need to allow for electronic verification systems becoming more common in the future.

We consider that this section should also take account of the verification of identity already conducted by a bank when a new facility is established with a payment by a personal cheque in the same customer name. This is acknowledged for enhanced monitoring purposes in paragraph 54 of the discussion document which states: “...reporting entities may consider whether the funds paid into the account originate from a recognised financial institution that is subjected to appropriate AML/CFT laws...”. The reported back Bill does not appear to allow for that situation in the CDD process.

We note also that the reported back Bill does not include a consequential amendment to sections 203 and 204 of the KiwiSaver Act which refers to verification of identity under the Financial Transactions Reporting Act. It would be useful to have an explicit exemption for default KiwiSaver members in the regulations.

Customer Due Diligence for Existing Customers

We note that the reported back Bill has taken a more risk-based approach to the requirement to conduct standard due diligence in relation to existing customers. We endorse the amended approach.

Ongoing due diligence and account monitoring

The ISI submission to the Select Committee expressed concern about the level of compliance involved in account monitoring, noting that it is potentially a major additional compliance burden which will add no value in the vast majority of cases and does not take account of the level of risk involved.

It would be helpful to have the regulations clarify the extent to which reporting entities can base their account monitoring on their assessment of risk and we welcome the view in paragraph 46 that the monitoring framework could focus on detecting exceptions (suspicious activities) rather than regular review of all activities.

Politically Exposed Persons

We welcome the exclusion of domestic PEPs from the reported back Bill. The Bill requires reporting entities to ‘take reasonable steps to determine whether the customer or any beneficial owner is a politically exposed person.’ The discussion document proposes elements of a PEP management framework and it would be useful to have expectations set out in regulations.

Beneficial Ownership

Paragraph 78 of the discussion document acknowledges that the definition of beneficial owner is intended to require ownership or control and it is not intended to include the beneficiaries of discretionary trusts. However, paragraphs 79 to 81 suggest regulations will be drafted so as to require the identification of a number of non-control beneficiaries. We would not support such a requirement being introduced by regulation.

Use of third parties in CDD

The reported back Bill has been amended in respect of reliance on members of a designated business group but there has been no change to section 29(1)(a)(ii) which requires CDD information to be held by each entity in the group that establishes a business relationship with the customer. Financial services groups typically consist of a number of funds, trusts and other entities (e.g. unit trusts, superannuation schemes, KiwiSaver funds, life insurers) that will all be reporting entities. Records, including CDD, will typically be held centrally and it is therefore inefficient to duplicate verification information across reporting entities within the group.

We recommend that the regulations should be drafted to enable verification information to be held by one reporting entity within the reporting group.

Exemptions

New section 4A in the reported back Bill will limit the range of activities within reporting entities that come within the definition of financial institution.

As noted above, we support the view that certain low risk products should be considered for an “exemption due to unnecessary capture”. The example given in paragraph 34 of

the discussion document should certainly apply to KiwiSaver (locked in until at least age 65 or for 5 years, whichever is the later date).

In addition, we support the proposal in paragraph 34 and, in particular, examples 34.1 and 34.2.

Conclusion

Our general conclusion is that the amendments made by the Select Committee have improved the Bill but there are still a number of areas in which the regulations need to provide further clarification.

We strongly support the Select Committee's comments in respect of risk assessment and harmonisation with Australia. We would particularly like to see clarification in the regulations that treatment of pure risk insurance on a similar basis to the Australian regime would be acceptable.

Yours sincerely

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Chief Executive