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FEATURE ARTICLE

AML/CFT Act Phase 2 — Accountants captured

Introduction

Money laundering is a process where "dirty money" received from criminal activities, such as misuse of drugs, theft and tax evasion, is passed through legitimate businesses and turned into "clean money". Terrorism financing uses similar methods to money laundering to channel funds to violent causes.

Background

The Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (AML/CFT Act) has placed obligations on financial institutions and casinos to comply with its requirements since 2013 (Phase 1). Additional New Zealand businesses have been or are now preparing to be caught by the AML/CFT Act (Phase 2).

It is estimated that about $1.35b from fraud and illegal drugs is laundered in New Zealand each year. Tax evaders and international and local criminals try to launder funds through New Zealand businesses and New Zealand is also exposed to threats relating to financing of terrorism.

On 10 August 2017, the Anti-Money Laundering and Countering Financing of Terrorism Amendment Act 2017 was passed and brings lawyers, conveyancers, accountants and real estate agents (collectively known as Designated Non-Financial Businesses or Professions (DNFBPs)) into the existing AML/CFT Act (Phase 2).

Part of the reason for extending the AML/CFT regime to the Phase 2 sectors is to bring New Zealand into line with international best practice and help maintain public and business confidence in New Zealand's overall financial best practice. New Zealand, being a member of the Financial Action Task Force (FATF), requires certain business activities within the Phase 2 sectors to be brought within the AML/CFT Act.

The Department of Internal Affairs (DIA) is the AML/CFT supervisor for the Phase 2 entities.

Accountants will have to comply with the AML/CFT regime from 1 October 2018.

Why does the AML/CFT Act apply to accountants?

Services provided by accountants are often used by criminals to hold and move assets and funds anonymously.

Introducing AML/CFT measures will deter criminals from using accountants' services and help detect them if they do.

It will also strengthen the overall AML/CFT system. For example, an accountant may detect "red flags" that might not be picked up by banks or other financial service providers who interact with the same customers. That's because accountants may have more information about the people or funds involved in a particular transaction.

Accounting practices captured under the AML/CFT regime

The AML/CFT Act is activity-based. An accounting practice is a reporting entity and needs to comply with the AML/CFT regime if, in the ordinary course of business, it carries out one or more of the following activities (see s 5(1) "designated non-financial business profession" (DNFBP)).

(Note: the information in the table below is largely extracted from the Accountants Guideline (March 2018). The examples are illustrative and not exhaustive).

Captured activities	Example of accounting service
Act as a formation agent of legal persons or arrangements.	• You register a company with the Companies Office on behalf of your client. • You form an incorporated society on behalf of your client. See Accountants Guideline, p 14.
Act as, or arrange to act as, a nominee director, nominee shareholder or trustee of a trust in relation to legal persons or legal arrangements.	• You act as a nominee director or a nominee shareholder of a company. • You arrange for a person to act as a nominee shareholder for a company. • You act as a trustee for a trust. See Accountants Guideline, p 15.
Provide a registered office, business address, correspondence address or an administrative address for a legal person or legal arrangement (unless that service is provided solely as an ancillary service to the provision of other services that are not captured activities).	• You provide a sole trader with a business address as its registered office address but you do not provide any other services. See Accountants Guideline, p 15.
Manage client funds (other than sums paid for professional services), accounts, securities or other assets.	• You operate a trust account. • You have the authority to make payments on behalf of your client's business directly from their bank account. • You make investments on behalf of a client in securities and/or other assets using funds from their bank accounts which you have authority to transfer. • You manage the sale and/or purchase of trust assets for your customer using funds from their bank accounts which you have the authority to transfer. • You disburse the funds generated from a company's insolvency liquidation to a creditor in line with the relevant administration requirements. • You exercise the enduring power of attorney which you hold for a client who has lost mental capacity by making payments from their personal bank account to meet their financial obligations. See Accountants Guideline, pp 15 and 16.
Engage in, or give instructions on behalf of a client to another person for, transactions in relation to buying, transferring or selling, or creating, operating or managing a business, legal person or legal arrangement.	• You instruct a conveyancer to effect the sale of a house owned by your client. • You purchase farm land as a trustee (together with other trustees) for your client's family trust. • You give instructions to a nominee overseas to purchase a company for that client in that country with funds provided by the client. • You instruct a trust and company service provider to transfer funds provided by your client to the bank accounts of a newly formed company or for which your client is the sole shareholder. See Accountants Guideline, pp 16 and 17.

Accounting services not captured under the AML/CFT regime

Some examples of accounting services that will not be captured include:

- Conducting a captured activity in your personal capacity (as opposed to in your professional capacity).

  Example: You are a trustee of a registered charitable trust in your local community in your personal capacity.

- Advice alone.

  Example: You regularly provide your client with advice about payments they should make (eg for tax or payroll) but you never control the flow of funds yourself.

- Auditing and assurance services.

  Example: You provide financial auditing and other assurance services to clients who are only requesting these kinds of services. Similarly, if you are requested to provide AML/CFT auditing services to businesses that, by virtue of their being either a financial institution or a DNFBP, are required to comply with the AML/CFT Act.

- Loading payments on behalf of your client.

  Example: You load payments that are then approved by the client, but you do not control the funds. However, if you are authorising payments from your client's account directly into their staff or suppliers' accounts, you are controlling the funds and this will be a captured activity under the AML/CFT Act.

  The key determining factor especially when managing client funds is whether you have control over the flow of funds — if you do have control, your activity is captured. For example, in a payroll situation, if you are loading payments that are then actioned by your client, you are not controlling the funds, your client is. However, if you are authorising wage and salary payments from your client's account directly into their staff's personal accounts, then this is a captured activity.

  Activities or services must be done in the ordinary course of business to be captured by the AML/CFT Act. Whether an activity is done in the ordinary course of business will be a matter of judgement depending on the nature of your business.

What does a reporting entity need to do to comply with the AML/CFT Act?

Appoint a compliance officer (s 56) (see Accountants Guideline, p18)

This is a critical role that reports to senior management. The compliance officer is responsible for administering and maintaining the AML/CFT programme and liaison with the AML/CFT supervisor. The compliance officer must be committed to the position and be the right person!

They must have a good understanding of the business and influence within the business. In the case of a sole practitioner, the DIA would expect the sole practitioner to be the compliance officer. If that is not possible, an external person must be appointed as a compliance officer.

Conduct a risk assessment (s 58) (see Accountants Guideline, pp 18, 19)

Reporting entities are required to undertake a written assessment of the risks posed to their business by money laundering and financing of terrorism crimes. To conduct a risk assessment you need to assess the business and identify the ML/FT risks that may be faced in the ordinary course of business. When conducting a risk assessment, it is important to use what you know — your hands-on experience and history of the business. The DIA have not provided templates but has provided guidance on its website: Risk Assessment and Programme: Prompts and Notes for DIA reporting entities (December 2017) and Phase 2 AML/CFT Sector Risk Assessment 2017 (December 2017).

Risk assessments are required to be regularly reviewed and updated where there is any material change to the business, its service offerings, or its client base, or where deficiencies in the effectiveness of the risk assessment are identified. The risk assessment is a living process — not a one-off!

Develop an AML/CFT programme (s 57) (see AML/CFT Programme Guideline, p 19)

The AML/CFT Act requires that accounting firms have regard to guidance produced by the supervisor when developing their AML/CFT programme (s 57(2)). The Supervisors' guidance on developing an AML/CFT programme is available on the DIA website (AML/CFT Programme Guideline).

The AML/CFT programme must be in writing and based on the risk assessment. It should include procedures, policies and controls around:

- vetting of senior managers, the compliance officer and any other employee that is engaged in AML/CFT-related duties
- training on AML/CFT matters for senior managers, the compliance officer and any other employee that is engaged in AML/CFT duties
- complying with Customer Due Diligence (CDD) requirements (including ongoing CDD and account monitoring)
- reporting suspicious activities
- reporting prescribed transactions, and
- record-keeping.

Ongoing compliance requirements

• Conduct CDD before entering into a business relationship or conducting an occasional transaction (see Accountants Guideline, pp 23–34).

There are three levels of CDD — standard, simplified, enhanced.

The key elements are:

— Identification and identity verification.

— Nature and purpose of business relationship.

— Identity of beneficial owners.

For enhanced due diligence:

— Source of funds or wealth.

— Verify this information according to level of risk.

For new customers, accounting firms will need to establish at the outset whether they are going to require the firm to conduct any activity captured by the AML/CFT Act. If they are, the firm will need to conduct CDD in line with the level of risk anticipated and in accordance with the requirements in the AML/CFT Act.

CDD must be conducted on existing customers if there has been a material change in the nature or purpose of the business relationship with that customer, and/or there is insufficient information about that customer.

• Submit a Suspicious Activity Report to the Financial Intelligence Unit (FIU), if there are reasonable grounds to suspect that an activity may be relevant to the investigation or prosecution of an offence (see AML/CFT Programme Guideline, p 21).

• Submit a prescribed transaction report to the FIU when a client conducts one of the following through the reporting entity:

— a domestic physical cash transaction of NZ$10,000 or more, or

— an international wire transfer of NZ$1,000 or more.

• File an annual report with the DIA (see AML/CFT Programme Guideline, p 29). The report will be submitted to the DIA electronically and includes questions about the number of customers, transactions, etc. The first report is due between 1 July and 31 August 2019. A user guide will be available in preparation for the report.

• Obtain an independent audit of the risk assessment and AML/CFT programme every two years by an independent and appropriately qualified person (see AML/CFT Programme Guideline, p 20).

• Retain records of documents associated with transactions (including the nature, amount, currency date and parties involved, for not less than five years) (see AML/CFT Programme Guideline, pp 19, 20).

First civil proceedings filed by the DIA under the AML/CFT Act

There are two cases where the DIA has filed civil proceedings in the Auckland High Court against Auckland-based money remitters under the AML/CFT Act (see *Department of Internal Affairs* v *Ping An Finance (Group) New Zealand Company Ltd* [2017] NZHC 2363 (Ping An) and *Department of Internal Affairs* v *Qian Duoduo Ltd* [2018] NZHC 1887) (QDD). Both were "reporting entities" under the AML/CFT Act.

Although the cases had heavily contrasting facts, both involved determination of appropriate pecuniary penalties for civil liability acts in terms of the AML/CFT Act.

QDD was the first defended case under the AML/CFT Act.

QDD is a financial services provider specialising in foreign currency transactions and international money transfers. QDD had accepted liability that it failed to comply with its responsibilities under the AML/CFT Act and the DIA sought a "civil pecuniary penalty" in respect of each of four breaches of its duties to undertake: risk assessments; enhanced due diligence; customer due diligence; account monitoring; and record-keeping.

The DIA sought pecuniary penalties of $2.6m. However, the High Court found liability at the lowest end and accepted that QDD had genuinely tried to comply with the AML/CFT Act and had relied heavily on advice provided by a consultant. The Court also recognised that some of the AML/CFT Act's requirements were confusing and it was understandable that QDD had misunderstood some of its obligations. The Court imposed a penalty of $356,000 on QDD.

The QDD case is very important for anyone trying to comply with the AML/CFT Act, as is Ping An, the only other prior undefended case.

The facts of QDD contrast heavily with the facts of Ping An, an undefended civil claim brought by the DIA where penalties of $5.29m were imposed as well as ordering that the company and its sole director and shareholder not undertake any financial activities.

Ping An, a money remittance and foreign currency service provider, had committed numerous civil liability acts, including failure to carry out customer due diligence checks and failure to adequately monitor accounts and transactions and report suspicious transactions in breach of the AML/CFT Act. These were flagrant breaches with total disregard to the compliance requirements under the legislation.

The Court agreed with the DIA submission that the failures were at the "higher end of non-compliance with the Act's requirements". Justice Toogood said that the penalties he imposed "must be so significant as to deter and denounce non-compliance" and recognise Parliament's intention that tougher penalties should be awarded than under previous legislation.

In both cases, the Court was not alleging that Ping An or QDD were involved in money laundering or the financing of terrorism, but that they failed to meet the legislative requirements.

Lessons to be learnt

The High Court's decision in QDD is significant as it indicates that a reporting entity's clear intention to comply with the AML/CFT legislation is a significant mitigating factor in sentencing. Ping An had been an undefended case where serious compliance issues with no real explanation for them had been raised. Ping An had made no attempt to comply with the legislation at all. In contrast, QDD had made considerable attempts to comply with the legislation but unfortunately had been poorly advised by its consultant.

Although these proceedings did not involve accounting practices, the lessons can be applied to all reporting entities that carry out captured activities under the AML/CFT Act.

OTHER MATTERS

Overseas buyers ban receives Royal assent

The Overseas Investment Amendment Bill (Amendment Bill) was given Royal assent on 22 August 2018 and takes effect on 22 October 2018 (Overseas Investment Amendment Act 2018) (Amendment Act). The new law restricts certain overseas people from buying residential land in New Zealand. The Overseas Investment Amendment Act Regulations 2018 to support the Amendment Act have been published. They too will take effect on 22 October 2018 (immediately after the Amendment Act).

"This is a significant milestone and demonstrates this Government's commitment to making the dream of home ownership a reality for more New Zealanders", Associate Finance Minister David Parker said.

(Source: www.beehive.govt.nz)

Background

Foreign investment forms a significant part of our economy and brings benefits to New Zealand. The Overseas Investment Act 2005 (Act) aims to balance the privilege of owning sensitive assets in New Zealand against facilitating the flow of overseas investment to the country. It does this by requiring overseas investments in sensitive assets, before being made, to meet criteria for consent and imposing conditions on those overseas investments.

Under the Act, an overseas person wanting to invest in "sensitive" New Zealand land must satisfy the Overseas Investment Office (OIO) that the investment is likely to be of benefit to New Zealand. For rural land, that benefit must meet a higher threshold of being "substantial and identifiable". "Benefit" is assessed against specific factors listed in the Act and Regulations.

The Act provides that an overseas person does not currently need OIO consent to buy residential property in New Zealand (unless it has "sensitive" features, such as historic heritage status, or adjoining a reserve).

Why is the Act changing?

The Government says the changes relating to residential land are designed to stop foreign speculators buying houses which would otherwise be available for New Zealanders. It is an attempt to make housing more affordable (on the assumption that foreign buyers are driving up prices).

Overseas Investment Amendment Act 2018

In December 2017, the Government introduced the Amendment Bill. The main focus of the Amendment Bill was to bring "residential land" within the category of "sensitive land", with the purpose of creating a housing market with prices shaped by, and making homes more affordable for, New Zealand buyers. It was also to restrict the acquisition of residential land by overseas investors, so that any such investment made by overseas persons will have genuine benefits for the country; effectively banning anyone who is not a New Zealand citizen or resident from purchasing residential land.

There are some notable exceptions to this.

You are not an "overseas person" (and don't need to apply for consent) if you are a residence class visa holder who:

- has been living in New Zealand for at least 12 months before the purchase
- has been present in New Zealand for at least 183 days of that time, and
- are a New Zealand tax resident.

Overseas persons will be able to buy sensitive land that is residential land in certain situations, if they:

- will be developing the land and adding to New Zealand's housing supply
- will convert the land to another use (eg a business) and are able to demonstrate this would have wider benefits to the country, or
- have an appropriate visa status and can show they have committed to reside in New Zealand (the criteria for this will be defined through regulations).

Conditions will be imposed if an overseas person purchases residential land utilising one of these exemptions. For example, if an overseas person purchases residential land for development, they will be required to on-sell the new houses that they build.

The OIO is to be given powers to dispose of land where a person in relation to property has contravened the Amendment Act, committed an offence, or failed to comply with a condition of consent or of an exemption.

Detailed information and guidance on the changes will be available on the OIO website by early October, and applications for consent will open once the Amendment Act takes effect on 22 October 2018.

Other information

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