Anti-money laundering and the struggle with risk-based legislation

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Agenda

1. The AML/CFT Act
2. Risk-based Approach – Benefits & Challenges
3. Observations

The Act

The AML/CFT Act sets out the high level obligations and responsibilities on reporting entities including:

- Developing and maintaining a risk assessment
- Developing and implementing a risk-based AML/CFT programme

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The Act

- Increased customer identification and verification (know who your customers are, i.e. beneficial ownership and who exercises control)
- Ongoing customer due diligence and transaction monitoring
- Enhanced suspicious transaction reporting (STR)

The Act

- Improved record keeping requirements
- Employee vetting and training
- Independent auditing
- Annual reporting

The Act – Risk Assessment

Must have regard to the following:

a) the nature, size, and complexity of its business

b) the products and services it offers

c) the methods by which it delivers products and services to its customers

The Act – Risk Assessment

d) the types of customers it deals with

e) the countries it deals with

f) the institutions it deals with

g) any applicable guidance material (e.g. Sector Risk Assessments)

A Risk-Based Approach

- Not a NZ invention.
- Based on international guidance, primarily Financial Action Task Force (FATF).
- See FATF's 'Guidance on the Risk-based Approach to Combating Money Laundering and Terrorist Financing - *High Level Principles and Procedures*', June 2007

A Risk-Based Approach - Benefits

- More efficient and effective use of limited resources
- Minimise burden on customers
- Makes it more difficult for criminals to launder due to:
  – increased focus on high risk activities
  – adapt more quickly

A Risk-Based Approach - Benefits

"An effective risk-based approach will allow financial institutions to exercise reasonable business judgment with respect to their customers."

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A Risk-Based Approach - Challenges

A range of reporting entities:

- FMA - issuers of securities, trustee companies, futures dealers, collective investment schemes, brokers, and financial advisers – 707 entities
- RBNZ - banks, life insurers, and non-bank deposit takers – 60 entities

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A Risk-Based Approach - Challenges

- DIA - casinos, non-deposit taking lenders, money changers, and other financial institutions not supervised by the FMA or RBNZ – 862 entities

A Risk-Based Approach - Challenges

- Subjectivity leads to uncertainty
- Need for expertise
- Staff uncomfortable making risk-based judgments:
  - Overly cautious
  - Disproportionate time spent
- Risk assessments are not static

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A Risk-Based Approach - Challenges

- Supervisors and auditors:
  - A number of solutions to the same “problem”
  - Not a pass/fail exercise
  - Guidance may need to be high level to accommodate a number of approaches
  - Specifically, auditors are not expected to audit the judgment calls made in the risk assessment

Observations

- Not capturing all applicable products
- Not excluding exempt products
- Not including enough detail
- No consideration of Sector Risk Assessments
- Risk assessment doesn't flow through to the Programme

Observations

- Methodology:
  - Framing of risks
  - Overly complex methodology
  - Explaining risk levels

Observations

- "De-risking":

  "A risk-based approach should not be designed to prohibit financial institutions from engaging with customers or establishing relationships with potential customers…"

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