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FMA
FINANCIAL MARKETS AUTHORITY
TE MANA TĀTAI HOKOHOKO - NEW ZEALAND

Class exemptions for managing intermediaries

This information sheet helps reporting entities understand the Anti-Money Laundering and Countering Financing of Terrorism (Class Exemptions) Amendment Notice (No 2) 2015 (Managing Intermediaries Exemption).

Overview

Under the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (AML/CFT Act), reporting entities have customer due diligence (CDD) obligations to identify and verify the identity of their customers, the people acting on behalf of their customers, and any 'beneficial owners' of their customers.

Previous consultations on the CDD obligations of reporting entities have highlighted difficulties with the definition of 'beneficial owner' in the AML/CFT Act. While the current drafting is ambiguous, the Ministry of Justice and the AML/CFT supervisors agree the definition was intended to include:

- a natural person who owns more than 25% of a customer
- a natural person who controls a customer
- a natural person on whose behalf a transaction is conducted.

The phrase 'person on whose behalf a transaction is conducted' ('Powbatic') is a concept from the Financial Action Task Force (FATF) Recommendations. It is intended to ensure reporting entities can identify who is behind a transaction, when that person is someone other than the person(s) with actual or legal ownership or control of the customer. Paragraph 16 of the FATF *Guidance on Transparency and Beneficial Ownership* (October 2014) provides that:

> *"This element of the FATF definition of beneficial owner focuses on individuals that are central to a transaction being conducted even where the transaction has been deliberately structured to avoid control or ownership of the customer but to retain the benefit of the transaction."*

From this commentary, it is clear the concept of a 'person on whose behalf a transaction is conducted' is not intended to impose obligations on every possible natural person who may receive some benefit from a transaction occurring, but only to people who are 'central to a transaction being conducted'.

In 2013, the Financial Markets Authority (FMA) published an initial consultation paper outlining the practical implications of this definition of 'beneficial owner' in the managing intermediaries' context. This paper highlighted that where there is a chain of financial institutions/schemes involved in providing a service to an underlying client (the customers of a customer and/or the natural persons who are the end customers), an underlying client may be the 'natural person on whose behalf a transaction is conducted' and therefore a 'beneficial owner'. This means that all reporting entities in a chain of managing intermediaries will be obliged to determine whether such beneficial owners (who could be 'central to a transaction') exist and do CDD on those people, despite not meeting the threshold for actual or legal control or ownership.

Depending on the complexity of the legal structure, a reporting entity may be required to look through one or more financial institutions/schemes, and each reporting entity below it in the chain will be required to do the same.

The primary purpose of the managing intermediaries exemption is to reduce the compliance burden from multiple reporting entities in a chain of transactions having the same CDD obligations. This will also ensure that the CDD obligations fall on the reporting entity best placed to identify the customers' beneficial owners in any situation.

In essence, the exemption will, subject to certain conditions, exempt reporting entity 'A' from the requirement to look through managing intermediary customer 'B' to identify the person on whose behalf a transaction is conducted.

Entities that qualify for the exemption

For the exemption, a managing intermediary is a customer of a reporting entity that is a specific type of financial institution or managed investment scheme. The exemption creates two tiers of managing intermediary: licensed managing intermediaries, and specified managing intermediaries.

Licensed managing intermediaries

Part 4 of the exemption allows reporting entities to do simplified CDD (rather than standard CDD) on entities perceived as lower risk for AML/CFT purposes. These entities are defined as licensed managing intermediaries. This effectively exempts reporting entities from the requirement to do CDD on their licensed managing intermediary customers themselves, and any beneficial owners of those customers. However, reporting entities must still identify and verify people acting on behalf of the licensed managing intermediary according to sections 19 and 20 of the AML/CFT Act.

These entities are easily identifiable because they hold a verifiable status under a statutory regime. They are considered low-risk entities because of their level of regulatory oversight. They include:

- licensed non-bank deposit takers
- Financial Markets Conduct Act 2013 (FMC Act) participants subject to rigorous vetting processes (managers and supervisors of licensed managed investment schemes, other FMC Act licence holders, FMA appointees, and registered managed investment schemes)
- certain unit trust, KiwiSaver and superannuation schemes not yet transitioned to the FMC Act regime (those referred to in clauses 18(1), 34 and 35 of schedule 4 of the FMC Act).

It is not necessary to include NZ registered banks as licensed managing intermediaries because the simplified CDD provisions in the AML/CFT Act already apply to registered banks as customers.[1]

Conditions regarding licensed managing intermediaries

To rely on the exemption, a reporting entity must take reasonable steps to verify that the entity it is dealing with is a licensed managing intermediary. The status of a licensed managing intermediary will be recorded on an official register. For example, 'Disclose' records whether a particular scheme has been registered, and the Financial Service Providers Register records whether a particular entity has been licensed. It is sufficient to keep evidence that the appropriate register has been checked.

[1] See regulation 5 of the Anti-Money Laundering and Countering Financing of Terrorism (Requirements and Compliance) Regulations 2011

Specified managing intermediaries

Part 5 of the exemption applies to reporting entities whose customers are 'specified managing intermediaries'. These are financial institutions and schemes not subject to the same level of regulatory oversight as licensed managing intermediaries.

Under Part 5 of the exemption, reporting entities are exempt from the requirement in section 11(1)(b) of the AML/CFT Act to do CDD on certain beneficial owners of the specified managing intermediary (the Powbatics).

However, as these institutions are not subject to the same level of regulatory oversight as the licensed managing intermediaries defined in Part 4 of the exemption, reporting entities must still do standard CDD procedures on any beneficial owner who has effective control (such as a director), or owns more than 25% of the specified managing intermediary.

This lowered standard of CDD ensures there is still sufficient enquiry into the beneficial ownership of these specified managing intermediaries, while acknowledging these entities have their own reporting obligations under the AML/CFT Act and will therefore have carried out the required CDD on their own customer base. Specified managing intermediaries include:

- 'financial institutions' to which the AML/CFT Act applies, that are not licensed managing intermediaries
- foreign financial institutions that have their principal place of business in an overseas jurisdiction with sufficient AML/CFT systems and measures in place, and are supervised for AML/CFT purposes
- managed investment schemes and managers of such schemes that are not licensed managing intermediaries (such as an unlicensed manager of an unregistered managed investment scheme).

Entities not covered by the exemption

Financial advisers governed by the Financial Advisers Act 2008 who are not carrying out one of the roles described above, cannot currently be relied upon as specified managing intermediaries.

Conditions regarding specified managing intermediaries

Because specified managing intermediaries are not as readily identifiable as licensed managing intermediaries, reporting entities must carry out more checks on these customers before they can rely on the exemption. Specifically, the reporting entity must obtain written confirmation from a senior manager of the customer to the effect that it:

- has an AML/CFT programme in place (or a foreign equivalent)
- is supervised for AML/CFT purposes
- is doing CDD in accordance with the AML/CFT Act (or its foreign equivalent)
- has its principal place of business in a jurisdiction with sufficient AML/CFT systems and measures in place.

A senior manager of a specified managing intermediary refers to a senior manager to whom a reporting entity's AML/CFT compliance officer must report under section 56(4) of the AML/CFT Act, or a person holding a comparable position in foreign financial institutions.

If the entity is New Zealand-based, written confirmation of this is sufficient. To help ensure a foreign financial institution or scheme is in a jurisdiction with a sufficient AML/CFT regime, the New Zealand AML/CFT supervisors

have jointly published a Countries Assessment Guideline. The FATF also publishes lists of jurisdictions it considers to be non-cooperative and high risk, and lists of jurisdictions it continues to monitor. It is unlikely business from jurisdictions on these lists would qualify as entities with sufficient AML/CFT regulatory systems.

A reporting entity is not required to verify the written confirmation described above, unless there are reasonable grounds for the reporting entity to doubt the adequacy or veracity of the written confirmation.

Further points for relying on the exemption

Reporting entities must, on request, provide supervisors with the name of any customer who qualifies for the exemption.

The risk-based approach underpinning the AML/CFT Act applies equally to the exemption. Reporting entities must continue to do enhanced CDD on all managing intermediaries in accordance with the Act (for example, if any of the circumstances set out in section 22 of the Act apply, or if required under regulation 5A of the Anti-Money Laundering and Countering Financing of Terrorism (Requirements and Compliance) Regulations 2011). There are two exceptions to this obligation:

- *Managing intermediaries that are trusts*

  The default position under sections 22(1)(a)(i) and (b)(i) of the AML/CFT Act is that reporting entities must do enhanced CDD on all customers that are trusts. However, the exemption overrides this requirement for managing intermediaries that are trusts. This is because a large portion of 'managing intermediary' customers will be managed funds, which are trusts. The purpose of the exemption would be defeated if these sections continued to apply to customers that are specified or licensed managing intermediaries.

  Any risk of money laundering or terrorist financing through customers that are trusts (and also licensed or specified managing intermediaries) is mitigated because all other circumstances triggering enhanced CDD will continue to apply.

- *Lower standard of enhanced CDD required under the exemption*

  In ordinary circumstances where a reporting entity is required to do enhanced CDD, sections 23 and 24(1) of the AML/CFT Act prescribe that the reporting entity must identify and verify any beneficial owner of that customer[2]. However, due to the level of oversight of customers managing intermediaries, even where circumstances trigger enhanced CDD, there is no requirement to identify and verify the Powbatics. However, reporting entities must continue to identify or verify any beneficial owner with effective control or who owns more than 25% of the licensed managing intermediary or specified managing intermediary.

[2] Sections 23 and 24 require reporting entities to identify and verify customers in accordance with sections 15 and 16 of the AML/CFT Act respectively. Sections 15 and 16 set out the identification and verification requirements with respect to the customers set out in section 11(1) of the Act, which includes *any* beneficial owner of a customer.

Flow chart of when the exemption would apply