Regulatory Impact Statement: AML/CFT Funding Model

Purpose of Document	
Decision sought:	Implement a levy to partially recover the costs of the regulatory system for Anti-Money Laundering (AML) and Countering the Financing of Terrorism (CFT).
Advising agencies:	Ministry of Justice
Proposing Ministers:	Hon Nicole McKee, Associate Minister of Justice
Date finalised:	26 September 2024

Problem Definition

The funding model for AML/CFT does not support an effective or efficient regulatory regime and is not aligned to cost-recovery principles.

Executive Summary

This Regulatory Impact Statement (RIS) should be read in conjunction with document "The supervisory structure of the anti-money laundering and countering financing of terrorism system" (Supervisory Model RIS). The Supervisory RIS sets the context for this paper and outlines how efforts to launder money and finance terrorism are expected to become more complex over time and require risk-based supervision across the economy.

The funding model for AML/CFT is currently uncoordinated and inflexible to new and emerging issues and opportunities. This has contributed to a regulatory system that is unable to take a whole of system approach to risk-based regulation.

The AML/CFT system is only able to apply a risk-based approach within the separate bounds set for each of the three current supervisors. Resourcing levels are similarly set within the bounds of each actor in the regulatory system, and their individual funding sources, rather than based upon the national risk environment.

Our funding model is also inconsistent with comparator countries, where cost-recovery typically funds most AML/CFT intelligence and supervisory activity. Only a relatively small proportion of our supervisory system is cost-recovered and the intelligence system is largely Crown funded.

The structural changes sought in the accompanying AML/CFT Supervisory Model RIS would best be supported by a funding model that is:

a. stable enough to implement a multiple-year risk-based work programme
b. flexible enough to reallocate resources anywhere in the AML/CFT system as national and sector risk assessments for ML/TF are updated
c. able to realise opportunities identified by industry and minimise compliance.

The model should also be consistent with principles for cost recovery and incentivise efficiencies by both reporting entities and government while achieving (a) to (c).

The work contributing to this RIS considered various options to unify the funding model for the regulatory system, including additional Crown funding or utilising the Proceeds of

Crime Fund. Those and other options were ruled out, with this RIS focussing on a pair of options based on cost recovery.

Options analysis in this RIS has found partial cost recovery through a levy provides the best way forward. This would part-fund the AML/CFT regulatory work of the Financial Intelligence Unit, Department of Internal Affairs, and the Ministry of Justice.

Based upon current regulatory expenditure, an upper limit for an AML/CFT levy for the preferred option is $23 million per annum. Ongoing Crown funding of public good aspects of the system would decrease this amount.

There are many details to work through with industry before the Stage 2 CRIS, but initial analysis is that the proposed levy would be able to be implemented without significant impact on industry. Industry reaction to the proposed levy is likely to be negative, however, an enhanced level of industry involvement in setting the levy-funded work programme could mitigate the level of negative reaction.

Limitations and Constraints on Analysis

The proximity to our next mutual evaluation (ME) by the Financial Action Task Force (FATF) in 2028 limits the time available for additional analysis and consultation to better inform decision-making in respect of legislative and funding changes.

High level costings for current regulatory services have been provided to inform this RIS, more detailed information will be needed to establish the amount to be cost-recovered.

The Ministry of Justice has not received requested qualitative risk assessment or quantitative information on reporting entities from supervisors that could be used to calibrate a levy. Reliance on publicly available information has an impact on the level of confidence able to be given in the CRIS on how the levy should/could be apportioned.

Industry have been consulted on the possibility of a levy for the AML/CFT regime, but this was limited and focussed on a flat fee rather than a differentiated levy. There are proposals to add levies on AML/CFT reporting entities for other regulatory regimes. These are at varying levels of certainty and design, so the cumulative impact is difficult to assess.

Responsible Manager(s) (completed by relevant manager)

Rajesh Chhana

Deputy Secretary - Policy

Ministry of Justice

26 September 2024

Quality Assurance	
Reviewing Agency:	Ministry of Justice
Panel Assessment & Comment:	**Document meets RIS quality assurance criteria** A Regulatory Impact Analysis Quality Assurance Panel from the Ministry of Justice reviewed the Regulatory Impact Statements for the supervisory structure and the funding model for the AML and CFT system. The Panel also reviewed the associated Stage 1 Cost Recovery Impact Statement. The Panel considers that the information and analysis *meets* quality assurance criteria. The Impact Statements are clear, comprehensive and make good use of the available evidence to build a convincing case. The Panel noted there were some limitations on consultation about the options for both the supervisor model and the funding model. However, consultation was undertaken on the broad approach and, within the constraints clearly outlined in the Impact Statements, the analysis can be relied on for decision-making. • All documents appear to be complete and have a clear problem definition. • The analysis is extremely thorough and the conclusions are supported by evidence or sound logic. Efforts have been made to address uncertainty. • All three documents are extremely technical and can be difficult to follow. However, this reflects the nature of the subject matter and the authors have attempted to address it to the extent possible. • There were some limitations on consultation about the options for both the supervisor model and the funding model. However, good consultation was undertaken on some options as well as the broad approach.

Section 1: Diagnosing the policy problem

1) What is the context behind the policy problem and how is the status quo expected to develop?

Current state

The Anti-Money Laundering and Countering the Financing of Terrorism (AML/CFT) system

1. The AML/CFT Act 2009 (the Act) plays a pivotal role in New Zealand's effort to combat serious and organised crime as well as terrorism by making it harder for illicit financial activity to occur. Undetected money laundering enables and incentivises offending that impacts the wellbeing of New Zealand communities and threatens New Zealand's international reputation.
2. Further, while the risk of large-scale terrorism financing in New Zealand is low, the consequences of lone actors self-raising funds can be devastating. There is also the risk that New Zealand becomes a conduit for layering or transferring funding for large-scale terrorism or proliferation in third countries.
3. The broader legislative framework and roles of the agencies involved in the regulatory system are set out in Annexes A and B respectively.

Resourcing of the system

4. Table 1 summarises information on current regulatory expenditure for AML/CFT. The AML/CFT regulatory system is majority Crown funded.

Table 1: System Resourcing 2024/25 (000's)

Agency	Funding source	Direct AML/CFT spend	Indirect AML/CFT spend[1]
Ministry of Justice (MoJ)	Crown funding	1,085	0
Department of Internal Affairs (DIA)	Crown funding	10,336 combined direct/indirect spend	
Financial Markets Authority (FMA)	Levy and Crown funding[2]	635	142
Reserve Bank of New Zealand (RBNZ)	RBNZ Funding Agreement	1,277	422
Financial Intelligence Unit (FIU)[3]	Crown funding	5,600	0
Total current spend		19,497	

Analysis has been limited to core AML/CFT regulatory entities.

[1] Indirect means supporting functions for the obligations under the Act, such as legal and communications teams. DIA has provided a combined estimate (only total costs).

[2] Approximately split of 83% levy and 17% Crown funding with a separate Crown-funded litigation fund which includes AML enforcement.

[3] The Financial Intelligence Unit is housed within NZ Police and is funded out of the broader Financial Crime Group. As its functions are distinct from wider Police work, and under international standards the FIU should be set up as an independent entity, we have looked at its resources separately from that of NZ Police.

2) What is the policy problem or opportunity?

The funding model does not support an effective or efficient regulatory regime

5. The funding model for AML/CFT is uncoordinated and inflexible to new and emerging issues and opportunities. This is flowing through to a regulatory system that is increasingly driven by operational silos and unable to take a whole of system approach to risk-based regulation.
6. Changes to Crown-funding also has an uneven impact across reporting sectors depending on who the supervisor is, rather than on a risk-based approach. The negative impact on system effectiveness of inconsistent funding settings was noted in the Regulatory Maturity Survey.[4]
7. The majority Crown-funding for a system that benefits industry or addresses an externality is also inconsistent with cost recovery principles. See problem definition in CRIS Stage 1 and Annex D for more detail on this issue.

The status quo will lead to negative economic impacts for New Zealand

8. The corresponding Supervisory Model RIS outlines in more detail the current state of ML/TF and how AML/CFT is expected to develop in New Zealand. To summarise, it is expected that ML/TF (and related proliferation financing) will become more sophisticated and outputs of AML/CFT system will need to adapt to this.
9. S9(2)(d)
10. S9(2)(d)
11. There are also wide-ranging economic impacts from an ineffective AML/CFT system.

The status quo will increase compliance costs and not realise opportunities

12. The level of mutual reliance by reporting entities and consumers in different AML/CFT reporting sectors is expected to increase. Digital enablers are rapidly evolving to increase payments and financial services flexibility, and we continue to reduce barriers to international investment and trade with key partners.
13. The system is not able to keep up with desirable change in the economy. This increases compliance burdens for legitimate business activity and impedes positive consumer outcomes. For instance, the Commerce Commission's study into retail banking competition found AML/CFT measures and their implementation detrimental to personal banking competition and financial inclusion. Its final report notes the considerable overlap of its own findings with those of the Statutory Review of

[4] Undertaken for the Act as part of a Statutory Review published in 2022Ministry of Justice (2022) *Report on the review of the Anti-Money Laundering and Countering Financing of Terrorism Act 2009*.

AML/CFT, and the lack of progress on its recommendations despite the competition and consumer benefits they would realise.[5]

3) What objectives are sought in relation to the policy problem?

14. The funding model for AML/CFT should be:

    a. stable enough to implement a multiple-year risk-based work programme

    b. flexible enough to reallocate resources anywhere in the AML/CFT system as national and sector risk assessments for ML/TF are updated

    c. able to realise opportunities identified by industry and minimise compliance.

15. The model should also be consistent with principles for cost recovery and incentivise efficiencies by both reporting entities and government [while achieving (a) to (c)].

---

[5] Commerce Commission. *Personal banking services,* Final Competition Report 20 August 2024. Page 295. Refer to the accompanying Supervisory Model RIS for more detail on the Statutory Review.

Section 2: Deciding upon an option to address the policy problem

1) What criteria will be used to compare options to the status quo?

Table 2: Criteria used to compare alternative options with the status quo

Criteria	What this means
Funding enables a risk-based approach.	The amount and allocation of funding for AML/CFT can change in line with the national risk environment.
The AML/CFT system aligns with cost-recovery principles.	At a system level, this would require efficient allocation of resources across the public and private sector and equity between the two (i.e. role of cost recovery in the system).
Feasibility.	Feasibility analysis will consider whether the option can be implemented: 1) within the current structure of the AML/CFT system, and 2) if the preferred option from the corresponding Supervisory Model RIS is progressed in tandem. Feasibility primarily relates to the need to implement improvements to our AML/CFT regime before our next ME by the FATF, in the context of resources at the Parliamentary Counsel Office and limited House time. Changes must be in place for two years for their effectiveness to be demonstrated and therefore considered as part of a ME by the FATF.

2) What scope will options be considered within?

Some funding models/options were ruled out

16. Cost recovery for the AML/CFT system is considered appropriate for three reasons:
    a. industry benefits from a well-regulated market that mitigates the impact on industry and its customers of the impacts of fraud in an effective and efficient manner,
    b. industry is enabling/creating a negative externality through their ordinary course of business, which should be mitigated and then any remaining cost internalised; and
    c. meeting FATF standards is a requirement for international financial and trade systems that provide direct benefits to reporting entities and their customers.

17. Additional Crown-funding was not evaluated as an option to cover the ongoing costs of supervision as it would not be consistent with cost recovery principles or provide desired incentives on industry or supervisor(s) to pursue efficiencies. The current model of majority Crown-funding of intelligence and supervisory functions is inconsistent with comparable countries as set out in paragraphs 28 to 32 below.

18. A levy-based funding model was given limited consultation through the Statutory Review. The Statutory Review model was based on each reporting entity paying $1,000 per annum. Industry feedback was that a flat fee would not reflect the difference in risk of ML/TF and benefits of AML/CFT across different reporting sectors and the entities within them. A flat fee or levy was therefore ruled out, and options for this RIS

were developed on the assumption that any payment would be weighted by relevant considerations to differentiate levy payers.

19. Cost recovery to provide a service to industry, or address a negative externality, can also be distinguished from cost recovery for a service that provides a discrete benefit to an identifiable person or entity (individual). Fees, rather than a levy, are not considered a viable option for substantive AML/CFT regulatory funding as they would create an incentive for reporting entities to avoid their AML/CFT obligations. This was also based on the experience in Australia, where a fees-based funding model was found to be impractical for reporting entities and had an excessive administrative cost. It created uncertainty of funding on a year-to-year basis and introduced additional complexity to setting cost recovery targets.

20. The use of Proceeds of Crime to fund the regime was discounted because of the incentives it would place upon a supervisor to seek 'revenue', and the level of uncertainty this would place on funding available for the regulatory work programme.

Extent of possible cost recovery

21. A key scope decision relates to the extent of public good funding that will continue to come from the Crown. In looking at the whole of the AML/CFT system, we consider that the roles of the supervisors, Financial Intelligence Unit, and the Ministry of Justice are responding to the negative externality enabled/created by industry, provide a service to industry, and are therefore within scope of cost recovery.

22. The roles of Police and the Ministry of Justice relating to other legislation within the AML/CFT system, most notably the Crimes Act and Criminal Proceeds (Recovery) Act, are criminal justice matters that are public goods not within scope of cost recovery.

23. The cost of prosecutions is similarly a criminal justice matter and any penalties awarded through the courts are returned to the Crown. The public/private split in terms of benefits of the AML/CFT regime, and how its costs should be borne, is discussed in more detail in the accompanying CRIS and will be better developed for its Stage 2.

Recent funding decisions on supervision for analogous regulatory functions

24. The Customer and Product Data Bill (CPDB) will give individuals and businesses greater choice and control over their data. It will require a 'designated' business to share customer data in a prescribed manner with accredited businesses. The CPDB will be introduced sector by sector, starting with the designation of banking products and data. The Bill allows for the introduction of a levy for each sector designated for inclusion in the scheme. It is proposed that levies will reflect the benefits or risks of operating in the designated sector. Some cost recovery may also occur through accreditation fees (accreditation is like licensing and involves registration).

25. The FMA also recovers the bulk of its funding from levies. In determining how to design its levy model, MBIE identified the following objectives:
    a. The cost of the levy for market participants is consistent with the benefits they receive from a well-regulated financial market;
    b. The levy will not discourage some classes of entity from supplying financial products or services; and
    c. The levy is practical in respect of its implementation, collection, and also avoids large over or under-collection.

26. All registered financial service providers (FSPs) must pay FMA levies annually. The FMA levy a FSP must pay depends upon the services it provides, and 'classes' of

service are then further delineated by either assets held, or revenue/fees received. A FSP must pay the full fee applicable for each class it is registered for (additive).

27. Recent funding decisions for both the External Reporting Board[6] and the Companies Office[7] have also implemented cost recovery from regulated entities on the basis that each provides a regulatory service for industry.

Relevant experience from other countries

28. Since the conclusion of the Statutory Review, which recommended looking into cost recovery options, the Ministry of Justice has undertaken consultation with Canada, the United Kingdom and Australia to better understand how cost recovery in their AML/CFT system works. The paragraphs below summarise the different systems, and commonalities across them. Annex C provides more details on the systems.

29. Canada's combined supervision and intelligence unit (FINTRAC) is entirely funded through cost recovery. The Department of Finance Canada and FINTRAC established guiding principles for FINTRAC's funding model, the first of which is that the funding model must generate sufficient funding for FINTRAC to administer its compliance program and the enabling internal services that support it.[8]

30. Australia's combined supervision and intelligence unit (AUSTRAC) is also entirely funded through cost recovery. Additionally, AUSTRAC undertakes some policy work (such as developing regulations) and provides Australia's delegation to the Asia-Pacific Group on Money Laundering (APG).

31. The United Kingdom recently implemented an Economic Crime Levy. This is an annual charge that levies entities (organisations) who are supervised under the Money Laundering Regulations and whose UK revenue exceeds £10.2 million per year. Funds raised through the levy do not go to specific regulators in set amounts, but instead to planned activities as outlined in the Economic Crime Strategy.

32. Key commonalities between overseas funding models were:

    a. Use of hybrid funding model to reflect creation of risk/vulnerability,
    b. Weighting of payments in accordance with risk, complexity, and profitability/revenue of payers,
    c. Accountability to industry on use of payments for support to industry in meeting their obligations, and
    d. Balancing fairness in apportioning costs and risk to reporting entities against administrative simplicity and efficiency in collection.

3) What options are being considered?

33. The Statutory Review (SR) considered the introduction of a hybrid public/private funding model for the regime through a 'flat fee' levy. A hybrid model was seen by the SR as having potential, as an industry contribution model would enable the regime to be more dynamic and responsive without being dependant on Crown appropriations.

34. Increased responsiveness could help ensure the regime would address compliance challenges at a faster rate, produce more comprehensive guidance, and make it easier for businesses to comply - and potentially reduce overall compliance costs.

35. Given existing compliance costs for industry, a levy was considered to need to demonstrate good value for money and deliver more responsive guidance, supervision,

---

[6] https://www.xrb.govt.nz/

[7] https://www.companiesoffice.govt.nz/

[8] Development and administration of the assessment of expenses funding model (canada.ca)

support, and regulatory reforms. The SR proposed that this could be achieved by basing any contribution from industry on a forward workplan agreed to between the private sector and public sector.

36. Most submitters to the SR opposed cost recovery. As mentioned above, there was particular opposition to a flat fee as the basis for cost recovery. Other points raised against cost recovery were that many reporting entities already paid a licensing fee, and that AML/CFT outcomes are a public benefit and the costs should be borne by government through general taxation. Similar arguments have been raised by a minority of industry stakeholders when the FMA levy is updated/increased.

37. Workshops conducted as part of the SR expressed less opposition to the proposal for a levy if it was determined by/for a collaborative work programme. The findings of the SR, and subsequent developments through targeted consultation with industry, have led to the development of two cost recovery options:

    1) Only cost of AML/CFT supervision, or
    2) Covering the AML/CFT cost of supervisors, FIU, and MoJ.

<u>Two key assumptions have been made throughout these options:</u>

38. **Assumption One:** any levy would be risk-based, with payment per entity within a levy band or grouping dependant on a range of criteria likely to encompass risk, complexity of supervision, and profitability/ability to pay. Size of entity would relate both to ability to pay and use of regulatory services.

39. **Assumption Two:** any levy for regulatory functions would replace rather than supplement current resourcing for that regulatory function. Crown-funding will be appropriated for the public good element of the AML/CFT regime. We have not assumed current expenditure at FMA/RBNZ would reduce on a 1:1 basis.

40. We note that this RIS is limited to an initial estimate of costs to be recovered under different levy options to understand potential (maximum) financial impacts on industry. If a new levy option is progressed, the level of 'sufficient' resources for cost-recovery would be more accurately calculated and consulted through the CRIS Stage 2 process.

41. In addition, the level of sufficient resources for supervision will be impacted by any decision to change the supervisory model or add to its work programme.

Option One – *Status Quo*

42. The status quo option sees the AML/CFT system being majority Crown-funded and subject to individual departmental/agency prioritisation. No additional Crown funding is anticipated as being available in the short-medium term.

43. The status quo does not meet criteria for enabling a national risk-based approach to resourcing or align with cost-recovery principles. The issues outlined in section 1(2) above will remain and objectives in section 1(3) will not be realised. The status quo funding model remains feasible with no structural change but, without additional Crown funding, would limit the progress of other options in the Supervisory Model RIS.

Option Two – *Levy for cost of supervision*

44. Option Two would see the cost of the supervisors delivering their regulatory functions under the Act as being majority levy funded. It would encompass direct supervision, enable functions (such as use of supporting intelligence, legal, and communications teams), and the supervisory component of international coordination.

45. This option would better enable risk-based supervision, but not address resource allocation across the wider regime. There would be a benefit to industry in terms of

improved support and reduced compliance as supervision has the most direct impact on reporting entities. Option Two will partially enable a national risk-based approach.

46. Recovering the costs of supervision would align with cost recovery principles as supervision is wholly responding to the externality of ML/TF and the service provided thorough the AML/CFT system. If risk-weighting of cost recovery through the levy is based upon residual risk, it also provides an incentive on industry to improve coordination and risk mitigation through new or improved systems/processes. Large banks would pay the largest individual fee, although the levy would apply across all high and medium risk sectors (refer attached CRIS for an illustrative table).

47. The three supervisors estimate current spend as just under $13 million per annum:

Table 3: Current AML/CFT Supervisory Annual Cost Estimate (000s)

	Direct AML spend	Supporting AML spend
DIA	10,336 direct and supporting spend	
FMA	635	142
RBNZ	1,277	442
TOTAL		**12,832**

48. To estimate what 'sufficient' resources for supervision might be, we have drawn upon the research undertaken when DIA became the supervisor for Designated Non-Financial Businesses and Professions. This costed both direct supervision and supporting spend, and included capacity to develop guidance for new sectors. For the RBNZ and FMA there is no research we can draw on to estimate sufficient resources, so have applied a 20% increase across supervisors to indicate approximate cost. This uplift would enable ongoing activity identified in the SR as required but not provided.

49. Total levy collection for Option Two on that basis would be approximately **$15.5 million per annum**. There may be a component of public good funding to be deducted from this amount (in the Stage 2 CRIS), so it provides an upper bound of cost impact for industry under this option with current cost data and stated assumptions as above.

50. Introducing the levy within the current structure of the AML/CFT system would necessitate amendment to legislation and regulations for the FMA and RBNZ. A suitable mechanism would need to be developed and implemented to allow for the raising and allocation of funding between the supervisors.

51. Ministers also have limited ability to direct the FMA and RBNZ on spending their allocated budgets or what work they are to produce in a specified time. Governance issues may preclude this option from being effectively implemented.

52. Unless there are changes to the supervisory structure, this levy will have a diminished impact on supporting good regulatory outcomes. The introduction of a levy would be consistent with, and support, a single supervisor model. It could be readily included alongside the legislative and regulatory changes that would be required to give the new structure legal effect.

Option Three - *Levy for cost of supervision, policy, and the FIU*

53. Option Three builds from Option Two, additionally including the costs of the MoJ and FIU in delivering their functions under the AML/CFT Act.

54. In addition to producing the National Risk Assessment, the FIU also provides support to industry through targeted guidance, briefings, and other information sharing. Legislative and regulatory change could also be better aligned with industry needs.

55. Integrating funding for the major functions of the AML/CFT Act would result in a more cohesive and coordinated approach to risk-based regulation – it will enable a national

risk-based approach to setting funding envelopes and allocating resources. Regulators and reporting entities will more effectively detect and deter ML/TF.

56. This option aligns with cost-recovery principles. It would also be applied on the basis of sector risk and firm size/ability to pay. The nexus of policy and the FIU with industry is lesser than with supervision but remains valid in the context of a cohesive regime providing risk-based regulation of AML/CFT.

57. Option Three will better enable the sort of differentiated and risk-based approach desired by the Commerce Commission in its market study of competition in retail banking. Similar benefits will be seen for other reporting entities and their consumers.

58. However, this option would require a higher amount of levy to collected. Estimated current expenditure is set out below.

Table 4: Current Annual FIU and MoJ Spend on AML/CFT (000's)

	Direct AML/CFT spend
Financial Intelligence Unit	5,600
Ministry of Justice	1,085
Total additional spend	**6,685**

59. In addition to the current costs outlined for Option Two and in Table 4:
    a. For the MoJ we estimate that resources of approximately $1 million per annum would be required to carry out all of these functions.
    b. For the FIU: a 20% uplift, in line with the estimate for supervisors.

60. Total levy collection for Option Three would be approximately **$23 million per annum**. There will likely be a component of public good funding to be deducted from this amount so it provides an upper bound of cost impact for risk-creating industry under this option with current cost data and stated assumptions as above.

61. This option was not specifically consulted on during the Statutory Review. Submitters were more receptive to a levy if it led to more support for them - which as outlined in section 1(2) is more likely to be delivered on by improved resourcing and integrated work planning across all of the functions that impact industry.

62. As with Option Two, introducing the levy within the current structure of the AML/CFT system would necessitate amendment to legislation and regulations for the FMA and RBNZ. A suitable mechanism would need to be developed and implemented to allow for the raising and allocation of funding between regulatory functions. Governance issues may preclude this option from being effectively implemented. The addition of MoJ and FIU will increase coordination costs and efficiency of implementation, but not detract from overall feasibility given their status as Crown agencies.

63. The introduction of a levy would be consistent with a single supervisor model and the changes that would be required to give the new structure legal effect. There will be

some additional complexity with the addition of MoJ and FIU but this will be required in any case to implement an effective national risk-based regime.

4) How do the options compare to the status quo?

	Option One – [*Status Quo / Counterfactual*]	Option Two – Levy for supervision as outlined in the Act	Option Three - Levy for supervision, FIU, and MoJ as outlined in the Act
Funding enables a national risk-based approach.	0	+ A single source of funding can be used as leverage to require higher levels of coordination and collaboration in supervision. Supervision will have sufficient funding flexibility to implement a risk-based approach. Other key functions will be subject to ongoing Crown funding decisions.	++ A single source of funding can be used as leverage to require higher levels of coordination and collaboration amongst AML/CFT regulators. Funding across the system will be able to adapt to a changing environment for ML/TF. Support for industry can be improved through the regulatory requirements for consultation on a levy.
The AML/CFT system aligns with cost-recovery principles.	0	+ Only applies to supervision, but supervision is the main point of interaction with industry. The closest direct connection/nexus with managing negative externalities and providing regulatory services.	++ The link of industry to other regulatory functions is not as close as with supervision, but that can be reflected in ongoing Crown funding. However, the other regulatory functions in AML/CFT are key elements of a risk-based approach to meeting the negative externalities created by industry and meeting FATF requirements, thereby still providing value to reporting entities and their customers.

	Option One – [*Status Quo / Counterfactual*]	Option Two – Levy for supervision as outlined in the Act	Option Three - Levy for supervision, FIU, and MoJ as outlined in the Act
Feasibility of implementation prior to next MER.	0	+ No barriers were identified to partial cost-recovery within required timeframes. The change in funding would need to be legislated and incorporated into the next funding agreement for the RBNZ and for the FMA in terms of both its Crown funding and levy collection. As there are existing mechanisms for both of these changes, the challenge will be in respect of structural issues as outlined in the Supervisory Model RIS.	+ Similar feasibility to Option Two. Drafting legislation and regulations will be slightly more complex than under Option Two. New appropriations may need to be added into Vote Police and Vote Justice.
Changes in analysis if single supervisor model adopted	0	++ Feasibility is improved under a single supervisor model and the legislative changes that will be needed to give it effect. A single levy for cost recovery would assist the implementation of a single supervisor.	++ Feasibility is improved under a single supervisor model and the legislative changes that will be needed to give it effect. A single levy for cost recovery would assist the implementation of a broader risk-based approach.
Overall assessment under status quo supervisor structure	0	+	++
Overall assessment with single supervisor	N/A	+	++

5) What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

64. Option Three best meets the criteria set in this RIS for an AML/CFT funding model under either the status quo structure or a single supervisor model. It is therefore the preferred option of the Ministry of Justice to enable a national approach to risk-based regulation that can adapt to changes in ML/TF and endure.

6) What are the marginal costs and benefits of the option?

65. The impact of non-monetised benefits has been determined from research undertaken and industry consultation during the Statutory Review. Following the Statutory Review, 6 months of co-design occurred with industry to understand the potential impacts on industry of options for legislative change.

66. This led to the finding that a lot of the impact/compliance cost comes from the lack of regulatory work in the areas that best support reporting entities and minimise unnecessary impacts on industry. A key example is the inability for the Ministry of Justice to process exemptions or more regularly review regulations to ensure opportunities for regulatory exemptions are being sought.

67. A key uncertainty in this analysis is exactly how the ML/TF environment will develop over the coming years. Whilst we expect the current trend towards increased sophistication of ML/TF, and therefore increased need of the AML/CFT system, this trend is difficult to predict. It is therefore uncertain how much the demands on the system are likely to change in coming years. Additional flexibility to the national funding of the AML/CFT system will help manage this uncertainty.

Table 5: Marginal costs and benefits of the preferred option

Affected groups	Comment	Impact	Evidence Certainty
Additional costs of the preferred option compared to taking no action			
Reporting entities	Public good component will be deducted from this amount	$23 million	Medium
Total monetised costs		$23 million	
Non-monetised costs	S9(2)(d)		
Additional benefits of the preferred option compared to taking no action			
Regulated groups	Additional support will be provided, an inherently more risk-based system that differentiates between reporting entities. Expected result is reduced compliance costs.	Medium/High	Medium – evidence from industry submissions and analysis in the Statutory Review, as well as looking at international experience, especially improved regulatory services in Australia once the work programme became levy funded.
Regulators	Levy-funded activity would otherwise be funded by regulators (avoided cost).	$23 million	Medium – expenditure impact on RBNZ and FMA not able to be determined at this point.
New Zealand	Sufficiently resourced system able to better detect and deter ML/TF, keeping New Zealanders safe from crime. Also reduced taxpayer burden.	Not monetised	Medium due to limitations in being able to estimate impact of AML/CFT on reducing crime beyond operational outputs, but can estimate current amounts of ML/TF (See 2024 NRA).
Total monetised benefits	Monetised costs and benefits are assumed to broadly offset		
Non-monetised benefits	Significant impact of an improved regulatory system	Medium	Medium

Section 3: Delivering an option

1) How will the new arrangements be implemented?

Legislation to enable levy setting and collection

68. Legislative amendment will be needed to provide the powers to set and collect an AML/CFT levy. Secondary legislation will also need to be passed to set more specific details of the levy and whom it will be collected from.

69. Consultation with industry on the best and fairest way to calculate payments will take place through the remainder of 2024 and potentially into 2025, with a Stage 2 CRIS bought to Cabinet in 2025.

70. This consultation would also include the best way to charge – whether through setting of transparent bands (like the UK) or charging individual invoices 6 months before payment is due (like Australia).

71. Industry have indicated a strong preference for a higher level of involvement in the setting and use of any AML/CFT levy than would be typical under standard levy settings. This is considered in more detail below.

72. S9(2)(f)(iv)

73. S9(2)(f)(iv)

74. There will also need to be a power to require reporting entities (some, or all) to declare financial details to the supervisor if relevant to the levy calculation.

Industry consultation and work programme reporting

75. We prose that the levy regulations specify how industry is to be consulted via two mechanisms – a National Strategy for AML/CFT, and a regulatory work programme.
    a. The National Strategy would outline trends in risks and direct existing resources to areas of highest risk and opportunity. It would include action items that are not levy funded – such as the target for asset recovery set in the last National Strategy.
    b. A regulatory work programme would be set to underpin the National Strategy. It would also be consulted with industry and publicly reported upon. This would include all relevant regulatory activities in the system, not just levy funded activity.

76. The National Strategy and regulatory work programme will inform decisions on the levy and Crown funding of AML/CFT. They will not change or set the level of levy being collected. Where the work programme requires a significant increase in work related to a regulatory function, agencies would need to outline the cost of that increase and corresponding impact on levy payers. Any changes in funding would need to be consulted on and approved through Cabinet (as with other levies).

77. The National Strategy should be revised every three years. This would allow the National Strategy to be set following a FATF Mutual Evaluation Report (MER), and give the regulatory work programme time to address its recommendations (and demonstrate effectiveness) in advance of the next MER.

78. Aligning levy collection with the delivery of a National Strategy means that the cost of compliance and need for adequate industry guidance will be factored into the regulatory work programme. However, the nature of the government role in AML/CFT

outlined in Section 1(1) means that it would not be feasible for industry to have veto powers over the work programme.

Giving effect to legislative changes

79. As the Ministry of Justice is already prescribed the role of advising on system outcomes and objectives, and its performance in achieving those, it would be a natural fit for the Ministry of Justice to be the agency responsible for developing the two levy mechanisms set out in paragraphs 75 to 78 (as per existing section 149 of the Act, in consultation with other agencies and with additional requirements on industry input).

80. The Ministry could also have a specified role to maintain an AML/CFT industry advisory group, including its amendment to ensure it remains representative across reporting entities, and that smaller reporting sectors can provide input. This would in the first instance be based on the existing industry advisory group, which has already conducted significant consultation and co-design work with the Ministry of Justice through the Statutory Review and development of legislative reform.

81. The mandate for coordination currently in the Act is too prescriptive and circumscribed. It is not flexible enough to be used for levy-making processes or reflect changes in the AML/CFT system or broader criminal justice sector. There is therefore a need to revise the mandate to:

    a. reflect the simplified operating environment enabled by a single supervisor,

    b. enable resource allocation across the AML/CFT system, and

    c. improve the ability of the coordination function to adapt and evolve.

Table 6: Outline of delivery timetable

Date	Milestone
October 2024	Cabinet agreement to cost recover
October – March 2025	Drafting of Bill
Commencing after November 2024	Consultation with industry on levy settings
August 2025	Bill enacted
TBC	Secondary legislation comes into effect (i.e. levy due for payment)

How will the new arrangements be monitored, evaluated, and reviewed?

82. As outlined above, the National Strategy and Annual Reports will provide ongoing monitoring, evaluation, and review of the AML/CFT system. This would include whether the agreed action items of the strategy are being met, as well as performance of core regulatory functions, and be a key input into any decisions on altering the levy.

83. The FATF will review the performance of New Zealand's AML/CFT system against the FATF standards every 7 years, with the next MER due in 2028-2029.

Annex A: New Zealand's AML/CFT regulatory regime

The AML/CFT Act 2009 plays a pivotal role in New Zealand's effort to combat serious and organised crime as well as terrorism by making it harder for illicit financial activity to occur.

In addition to the AML/CFT Act, the Crimes Act and Criminal Proceeds Recovery Act form the basis of the AML/CFT system. The AML/CFT Act sets out the broad system and its purpose, while the Crimes Act contains the offence of money laundering and CPRA provides ability for law enforcement to recover the proceeds of crime – including money laundering and any illegal activity undertaken to establish the funds to be laundered.

The AML/CFT system covers industry regulation (to deter ML/TF from occurring but also to detect and report suspicions of it occurring) through to criminal justice with investigations and prosecutions.

The administration, application, and enforcement of the of the AML/CFT system directly involves six agencies:

1. Ministry of Justice is responsible for administration of the AML/CFT Act 2009 (the Act). The role of the Ministry is set out in Section 149 of the Act and its stewardship responsibilities include advising the Minister of Justice as to whether any changes should be made to the regime.
2. The Department of Internal Affairs, Financial Markets Authority, and Reserve Bank of New Zealand are designated as AML/CFT supervisors. The functions and powers of the supervisors are set out in Sections 131 and 132 of the Act.
3. New Zealand Police is responsible for a variety of financial intelligence functions (set out in Section 142 of the Act) and powers (set out in Section 143 of the Act), including receiving reports from the financial industry [primarily Suspicious Activity Reports (SARs)] and disseminating financial intelligence products.
4. The Crown also separately funds the Financial Intelligence Unit (FIU in NZ Police) to co-operate with the supervisors, MoJ, New Zealand Customs Service (Customs) and any other relevant agency to help ensure the effective implementation of the requirements under this Act and regulations.
5. Customs does not explicitly have its functions outlined in the Act, but it is responsible for receiving reports of large movements of cash (over NZD 10,000) across New Zealand's borders.

The Ministry of Justice also forms the delegation to the Financial Action Task Force (FATF) and Asia-Pacific Group on Money Laundering (APG). The FATF is the inter-governmental body that produces a set of binding standards that countries are expected to apply when establishing their AML/CFT regimes, known as the FATF Recommendations. In addition to their other obligations under the Act, all agencies who form the regime are jointly responsible for making sure New Zealand fulfils its obligations as a member of the FATF and APG.

Annex B: Functions of agencies in the AML/CFT Act

Entity	Role in the AML/CFT system	Relevant Minister
Ministry of Justice (Public Service Agency)	Stewardship of the AML/CFT regime. Administers the Act, regulations and class exemptions. Leads engagement with the Financial Action Taskforce.	Minister of Justice
Department of Internal Affairs (DIA) (Public Service Agency)	Jointly responsible for supervision (including issuing jointly developed guidance, codes of practice).	Minister of Internal Affairs
Financial Markets Authority (FMA) (an independent Crown Entity)		Minister of Commerce and Consumer Affairs
Reserve Bank of New Zealand (RBNZ) (a statutory corporation)		Minister of Finance
New Zealand Police (Non-Public Service Agency)	Investigations, asset recovery.	Minister of Police
Financial Intelligence Unit (independent unit, housed in Police)	Receipt of Suspicious Activity and Prescribed Transaction Reports. Provision of Financial Intelligence to law enforcement and other agencies. Leads the National Risk Assessment.	Minister of Police
New Zealand Customs (Public Service Agency)	Receipt of Border Cash Reports.	Minister of Customs
Inland Revenue (Public Service Agency)	Key law enforcement partner.	Minister of Revenue
Serious Fraud Office (Public Service Agency)	Key law enforcement partner.	Minister of Police
Ministry of Foreign Affairs and Trade (Public Service Agency)	Administer autonomous sanctions, which put obligations onto AML/CFT reporting entities.	Minister of Foreign Affairs and Trade
Ministry of Business, Innovation and Employment (Public Service Agency)	Companies Registry, also Crown entity monitoring agency for FMA.	Minister of Commerce and Consumer Affairs

Annex C: AML/CFT cost recovery overseas

Australia[9]

Australia first introduced a levy to fund most of the work of AUSTRAC in 2011. AUSTRAC is a combined intelligence and supervisory entity (e.g. our FIU and three supervisors in one).

The structure of the levy has changed over time, following substantive reviews

Australia originally levied providers of designated services on a deemed-value 'user-pays' basis – calculated on factors including earnings and transaction values and volumes.

A new levy structure was applied to contributions in 2015. Compared with the original levy legislation, the 2014 amendments provided greater flexibility to change the levy structure by allowing more parameters (such as limits and thresholds) to be set via an annual Ministerial Determination. The amendments also required that the levy be independently reviewed four years after the amendment. None of the submissions to that review mounted substantial or substantiated arguments in favour of major changes to the levy arrangements.

In its present form, the Australian Levy Act does not prescribe any particular structure of, or basis for, the levy. However, the effect of the new structure was to shift more of the financial burden of the levy onto the largest reporting entities.

As a consequence of the combination of the adoption of a $1,000 minimum payment and the concentration of transactions reporting in a small percentage of reporting entities, the levy (at the time of the review in 2019) was paid by only 561 of the more than 14,000 entities reporting to AUSTRAC, compared with a total of 4,667 under the original levy regime.

Details on the current levy structure

The structure and details of the levy are set each year by a Ministerial Determination, following consultation between AUSTRAC and industry stakeholders. AUSTRAC initially publishes a stakeholder consultation paper that contains draft rates and thresholds within the levy structure that are expected to raise sufficient revenue to match the agency's cost recovery target. These rates and thresholds are refined on the basis of data received from reporting entities at the time of the annual census day.

The levy is not thought of as cost recovery, in the sense of a set of individual fees for service based on, or related to, identifiable costs of provision of that service. Rather, it is analysed as an industry-specific tax, calculated to recover AUSTRAC's operating budget. There is the significant caveat that, in meeting its revenue target, the levy should also be designed to minimise its regulatory burden (compliance costs).

As mentioned above, levy charges depend on entity earnings and the number and value of transactions reported by the entity to AUSTRAC. We understand from AUSTRAC that the latter is becoming an increasingly smaller factor in determining total payment amounts.

---

[9] Review of AUSTRAC Levy Arrangements

Coverage of the current levy

The result is that usually, only medium to large businesses are required to pay the levy. These are businesses with one or more of the following:

- earnings of A$100 million or more,
- a large number of transaction reports relative to other entities, and/or
- a high total value of transaction reports lodged with AUSTRAC during a calendar year, relative to other entities.

The distribution of the current basis for the levy (reported earnings and transactions report volumes and values) are highly concentrated in a small percentage of reporting entities. Modelling of revenue-neutral alternative levy parameters in the 2019 review demonstrated that there is considerable scope to redistribute the burden of the levy, albeit largely between currently liable entities. However it was also found that a more wide-spread distribution of levy contributions is likely to significantly increase total administrative and compliance costs.

United Kingdom[10]

The United Kingdom introduced an Economic Crime (Anti-Money Laundering) Levy (ECL) in 2021. The ECL was part of the government's wider objective to develop a long-term sustainable resourcing model to tackle economic crime. The ECL is an annual charge on entities who are supervised under the Money Laundering Regulations (MLR) and whose UK revenue exceeds £10.2 million per year (an estimated 4,000 businesses).

The ECL aims to raise £100 million per year from the MLR sector to pay for government initiatives outlined in the Economic Crime Plan (to help tackle money laundering). The Economic Crime Plan itself acknowledges the need for a long-term and sustainable resourcing model to transform the UK's response to economic crime.

As outlined in the Plan, the government believed that the resourcing model should comprise contributions from both the public and private sectors that participate in, and benefit from, the agenda to reduce economic crime. The ECL was seen as being fair and proportionate; as the firms most exposed to money laundering risk will be the principal financial contributors to the reform initiatives that will benefit them and help make the UK a safer place for them to do business.

The ECL is paid as an annual fixed fee. The amount of the fee is determined by which band the entity's UK revenue places them within. There are 4 band sizes:

ECL band size	UK revenue
Small	under £10.2m
Medium	£10.2 million to £36 million
Large	£36 million to £1 billion
Very large	more than £1 billion

[10] Levy Consultation Document - FINAL .pdf (publishing.service.gov.uk)

The fee for each entity within an income band is as follows:

ECL band size	ECL fee
Small	No ECL liability — not required to register with HMRC
Medium	£10,000
Large	£36,000
Very large	£250,000

<u>Canada</u>

Canada recovers the costs of supervision within its AML/CFT regime.

Recovering costs involves FINTRAC (our FIU and three supervisors in one) forecasting the full costs of its compliance program for the upcoming 3 fiscal years for inclusion in its Departmental Plan. This includes the costs of the enabling internal services that support the program such as human resources, information management/information technology (IM/IT), and communications, among others. This forecast then informs the estimated total cost that FINTRAC charges to reporting entities for the upcoming year.

FINTRAC holds a dedicated annual meeting with key stakeholders where it presents the key compliance program plans included in its most recent Departmental Plan. During this meeting, reporting entities can ask questions and seek clarifications on FINTRAC's forward-looking compliance agenda.

Every year, FINTRAC also produces an annual report which outlines how funds were spent against plans and priorities during the previous fiscal year. This information is included in FINTRAC's Departmental Results Report.

Guiding principles for the funding model

The Department of Finance Canada and FINTRAC established guiding principles for FINTRAC's assessment of expenses funding model:

- **Self-sufficient:** The funding model must generate sufficient funding for FINTRAC to administer its compliance program and the enabling internal services that support it.
- **Proportionate:** Reporting entities that have the greatest business volumes and are the most complex to supervise should be responsible for the majority of the cost.
- **Fair:** Charges for reporting entities with similar revenues and supervisory requirements should be consistent across sectors.
- **Efficient:** Administrative and information costs to calculate and collect charges should be minimized for reporting entities and FINTRAC.
- **Transparent and predictable:** Reporting entities should understand how the funding model works and the amounts they may be expected to pay.

Annex D: Regulatory Economics

A negative externality is the imposition of a cost on a party as a result of the actions of another party. In economics negative externalities arise when one party, such as a business, makes another party worse off, yet does not bear the costs from doing so. A negative externality may also arise from the consumption/use of a good or service. Pollution is often used to demonstrate both types of negative externality.

Using a motor vehicle as an example, pollution separately occurs in its creation ranging from mining raw materials through to powering the manufacturing plant that finally assembles it, then additional emissions and discharges over the use/life of the vehicle, and finally additional pollution in its dumping/recycling at end of life. The negative externalities follow the vehicle through its lifecycle, affecting a range of other parties to greater or lesser extents. Different regulatory regimes will often apply to the individual instances/sources of pollution.

In regulatory economics the government is considered to have a role to play in designing goods or services (and the associated charges) in a way that discourage actions with negative externalities. This includes things like ensuring a business is operating in accordance with regulations. Government intervention typically focusses on two groups:

1. people who benefit from the output of the regulated activity; and
2. risk exacerbators (that is, the individuals or organisations whose actions make it necessary for the government to become involved).

In this RIS, the primary activities under regulation are financial services, designated non-financial services, and other forms of value storage and transfer (domestic and international). Both consumers and providers benefit from the provision of these services. Providers are also risk exacerbators – their actions or inactions directly influence ML/CF outcomes for criminal and terrorist organisations and individuals.

Criminals undertaking predicate offending are targeted through the wider criminal justice system. The focus of the AML/CFT regime is on value flows after offending has occurred (provision and use). If value flows are successful criminal activity is incentivised, both through ability to reinvest in crime, and through the benefit of being able to realise and enjoy the profits of crime in the legitimate economy. For terrorism this allows the financing of terrorist activity.

In the case of incentivising crime and enabling terrorism, the negative externality affects the:

1. public through the occurrence of crime and terrorism
2. direct victims of crime and terrorism
3. legitimate businesses and consumers who may face increased sanctions/compliance
4. ability of service providers and industry to access international markets.

The AML regulatory regime is in place to allow legitimate value flows domestically and internationally while minimising illegal flows in as efficient and effective manner as possible.