

Money Remitters Left Out in the Cold: Blanket De-Risking Policies, Counterterrorism and Government Intervention in New Zealand

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The Anti-Money Laundering and Countering Financing of Terrorism Act 2009 was enacted to adopt international guidelines for combating money laundering and terrorism financing. An unintended consequence of the Act is the practice of commercial banks indiscriminately refusing to provide banking services to money remitters, citing compliance costs associated with the Act — while offering remittance services at a significantly higher price compared with money remitters. The 2016 High Court decision of E-Trans International Finance Ltd v Kiwibank Ltd found that such blanket de-risking policies were legal, but also that issues surrounding remittances were a matter of policy choices. This article explores the causes and consequences of blanket de-risking policies against money remitters and concludes that the New Zealand government should take legislative action. The suitable form of intervention depends on the desired result. If money remitters are to close and exit the market, the government must address the consequences of blanket de-risking policies: higher prices; the impact on economic and social development in recipient countries; and the proliferation of informal channels. If money remitters are to remain open, the risks posed by money remitters must be addressed. Regardless of the solution adopted, blanket de-risking policies should be addressed by the government because they have a negative impact on migrant communities and recipient countries, and can proliferate informal channels that facilitate financing of terrorism.

I INTRODUCTION

All acts of terror are financed. To operate, terrorist organisations require funding for operations, recruitment, training, salaries and social services.¹

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1 Financial Action Task Force *Emerging Terrorist Financing Risks* (October 2015) at 9–10.

The Financial Action Task Force (FATF) is an intergovernmental body that develops standards and guidelines to combat money laundering and financing of terrorism.² These guiding principles led the New Zealand government to enact the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (the AML/CFT Act), which imposes obligations on certain entities to report suspicious transactions and to implement Anti-Money Laundering and Countering Financing of Terrorism (AML/CFT) programmes.³

Counter financing of terrorism policies — like all counterterrorism policies — have led to unexpected consequences. For example, banks in New Zealand and abroad are adopting blanket de-risking policies where financial institutions terminate or restrict business relationships with clients or categories of clients. Money remitters — defined as non-bank companies that specialise in providing international and domestic money transfer services — have been targeted by these policies. This has resulted in the closure of money remitters due to their reliance on bank accounts to operate. Recently, in *E-Trans International Finance Ltd v Kiwibank Ltd*, the New Zealand High Court upheld the legality of blanket de-risking policies.⁴ In turn, the decision has raised questions about whether the government should intervene to discourage such policies.

This article explores the issue of blanket de-risking policies against money remitters and its implications for counterterrorism policy. It argues that the government should respond to the *E-Trans* decision. First, blanket de-risking policies and subsequent closures of money remitters negatively impact migrant families and developing countries that rely on remitted funds. Secondly, blanket de-risking policies encourage the use of informal, unregulated channels of remittance with higher terrorist financing risks. The government should intervene to ensure money remittances remain accessible, either by addressing the causes of blanket de-risking policies to enable money remitters to stay in business, or by mitigating the consequences of money remitter closures.

Part II will set out the background of the AML/CFT Act and the key actors and Part III will describe the issue of blanket de-risking policies. Part IV will explore the causes and motivations of blanket de-risking policies and Part V will outline the consequences of blanket de-risking policies. Part VI will cover the potential solutions the government may adopt, with references to approaches in comparable jurisdictions. I conclude that the New Zealand government should take legislative action. If money remitters are to remain open, the action should address the causes of blanket de-risking policies. And if money remitters are permitted to close, the consequences of blanket de-risking policies should be addressed.

2 Financial Action Task Force “About – Who we are” <www.fatf-gafi.org>.

3 Section 3(1)(b).

4 *E-Trans International Finance Ltd v Kiwibank Ltd* [2016] NZHC 1031, [2016] 3 NZLR 241.

II BACKGROUND AND KEY ACTORS

The AML/CFT Act

The AML/CFT Act and the AML/CFT regime reflect the tension between the public interest in countering terrorism through restricting its finances and the private commercial interest in supplying financial services to the market. The money remitting and banking industries mainly consist of private companies that require government intervention to meet the *public* objective of counter financing of terrorism, even at the cost of *private* profit.⁵ The relevant purposes of the AML/CFT Act are:⁶

- (a) to detect and deter money laundering and the financing of terrorism; and
- (b) to maintain and enhance New Zealand's international reputation by adopting, where appropriate in the New Zealand context, recommendations issued by the Financial Action Task Force; and
- (c) to contribute to public confidence in the financial system.

The AML/CFT Act reflects the FATF recommendations that emphasise a *risk-based approach*,⁷ where reporting entities are expected to assess their own risks of money laundering and financing of terrorism as well as those posed by their customers.⁸ Under this approach, reporting entities are required to adjust measures and customer due diligence — that is, gather and verify information on customer identity⁹ according to the level of risk.¹⁰ Enhanced measures are required for higher risk customers while simplified measures suffice for lower risk customers.¹¹ Reporting entities must ultimately achieve the following outcomes:¹²

- Knowledge of their customers' true identities;
- Monitoring of account activity;
- Identification of suspicious transactions; and
- Reporting of suspicious transactions to the Police.

Reporting entities under the AML/CFT Act include *financial institutions* in both the public and private sector.¹³ These encompass money remitters and banks as their services involve the acceptance of deposits from

5 Karen Cooper and Clive Walker "Security from Terrorism Financing: Models of Delivery Applied to Informal Value Transfer Systems" (2016) 56 Brit J Criminol 1125 at 1132.

6 Section 3.

7 See Financial Action Task Force *International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation: The FATF Recommendations* (February 2012) at 11.

8 Section 58.

9 "AML/CFT FAQs" Reserve Bank of New Zealand <www.rbnz.govt.nz>.

10 Financial Action Task Force, above n 7, at 31.

11 At 31.

12 The Treasury *Update on Remittances to the Pacific* (T2015/341, 12 March 2015) at Annex 2 (Obtained under Official Information Act 1982 Request to the Treasury).

13 Section 5.

the public, lending to or for a customer, and transferring money for or on behalf of a customer.¹⁴

The Ministry of Justice oversees the legislation and co-ordinates activities between the relevant government agencies, including the AML/CFT supervisors and the New Zealand Police. The AML/CFT supervisors are the Reserve Bank of New Zealand (RBNZ), Financial Markets Authority and Department of Internal Affairs (DIA).¹⁵

Remittance

Remittances are services provided to transfer money domestically and internationally. They enable foreign workers to send money to their home country. Remittances are especially important to people with limited or no access to banking services and to those relying on overseas family members for support. Remittance services enhance the welfare of workers' families and communities, as well as the welfare of their home country by bringing in foreign income. Small and medium-sized businesses may also rely on remittances to access new payment services for cross-border e-commerce.¹⁶ In developing countries, remittances from nationals overseas are more than three times the official development aid received;¹⁷ and, with the exception of China, remittances exceed foreign direct investment.¹⁸ Remittance flows are more stable compared to other external flows and, unlike capital flows, are not affected by interest rates or growth prospects.¹⁹

However, remittance services are vulnerable to facilitation of illicit fund transfers, including terrorist financing.²⁰ In Australia, for instance, the banking and remittance sectors are the most frequently used channels to send funds to suspected terrorist groups; and the Australian Transaction Reports and Analysis Centre (AUSTRAC), the regulator for AML/CFT responsibilities in Australia, attributes this to the sectors' ability to "move smaller amounts of money to jurisdictions where formal financial channels are less accessible".²¹

1 Money Remittance in New Zealand

Figure 1 shows estimates of remittance sent from New Zealand in 2014.²² Figure 2 shows, for the same countries, the size of remittance received as a

14 See s 5.

15 Section 130.

16 Kevin Davis and Martin Jenkinson "Remittances: Their Role, Trends and Australian Opportunities" (4 November 2012) Australian Centre for Financial Studies <www.australianceentre.com.au> at 1.

17 World Bank Group *Migration and Remittances Factbook 2016* (3rd ed, Washington DC, 2016) at 17.

18 At 17.

19 At 17.

20 Financial Action Task Force, above n 1, at 20.

21 Australian Transaction Reports and Analysis Centre *Terrorism financing in Australia 2014* (2014), at 7.

22 "Bilateral Remittance Matrix 2014" (October 2015) World Bank Group <www.worldbank.org>.

percentage of each country’s gross domestic product in 2014.²³ This indicates the importance of remittance to each country’s economy.

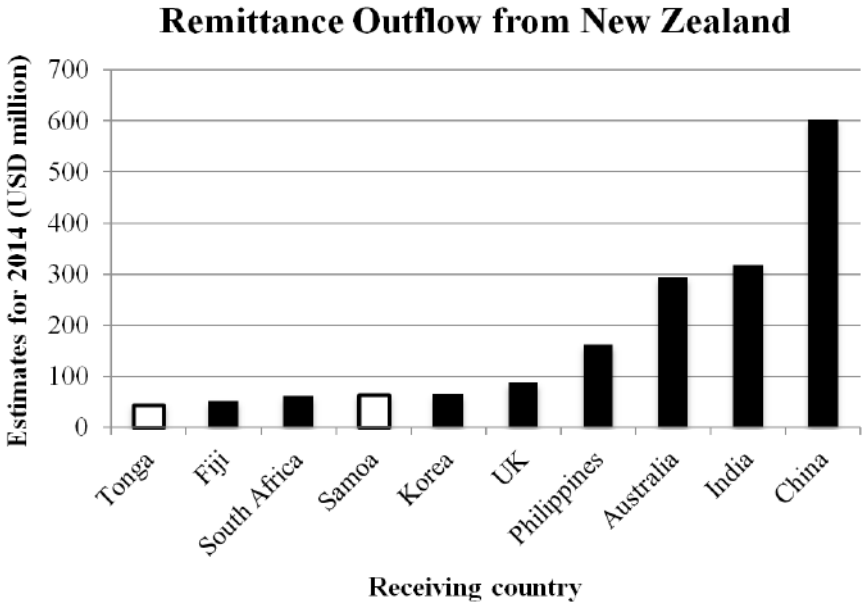


Figure 1: Remittance Outflow from New Zealand

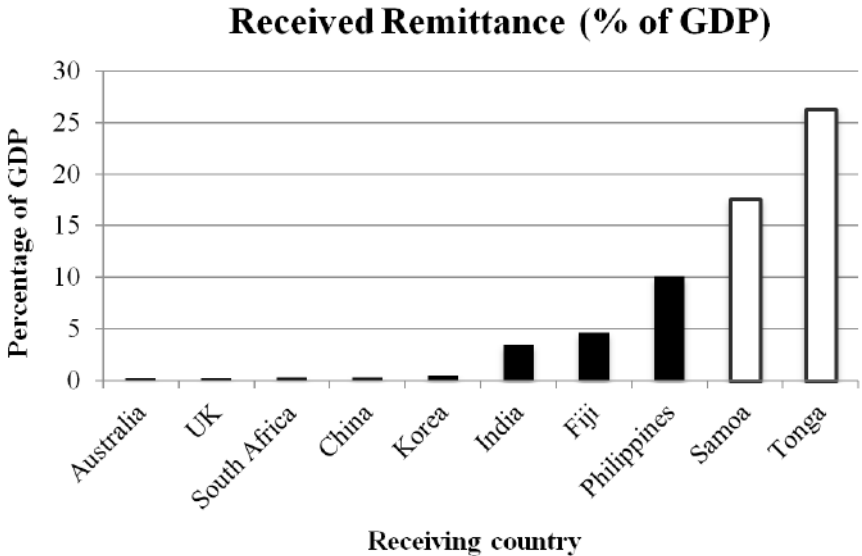


Figure 2: Received Remittance (% of GDP)

23 “Personal remittances, received (% of GDP)” World Bank Group <www.data.worldbank.org>.

The graphs highlight Samoa and Tonga to show the importance of remittance in their economies. The graphs also show the role played by remittance from New Zealand despite the relatively smaller outflow. Although Samoa, Tonga and Fiji make up less than six per cent of remittances flowing out of New Zealand, remittances from New Zealand make up a large proportion of GDP in Pacific countries.²⁴ This is supported by the finding that workers employed through the government’s Recognised Seasonal Employer Scheme send an average of 42 per cent of their take-home pay to their home country in the Pacific.²⁵ Tonga is particularly dependent on remittances — the fourth-most-dependent country in the world.²⁶

Although both banks and money remitters provide remittance services, their methods and costs differ. Figures 3 and 4 illustrate how money remitters and banks provide remittance services.²⁷

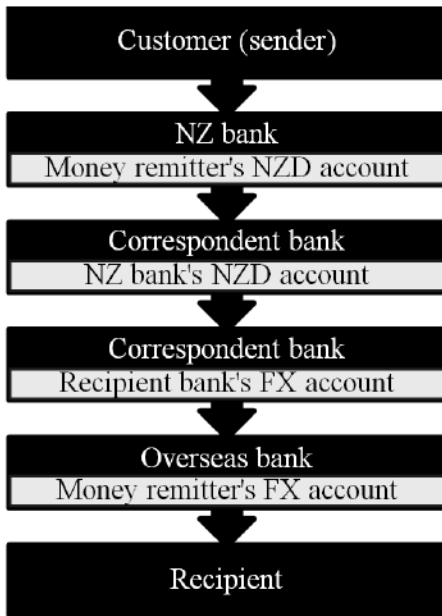


Figure 3: Money Remitters

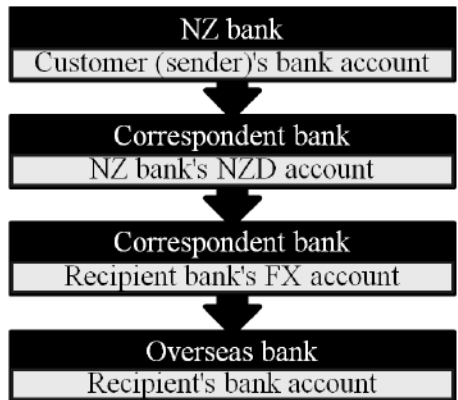


Figure 4: Banks

24 Deloitte *Review of the Money Remittance Market in New Zealand: A report on the problems affecting the remittance services between New Zealand and the Pacific* (The Treasury, August 2016) at [4.7].

25 Ministry of Business, Innovation & Employment *The Remittance Pilot Project: The economic benefits of the Recognised Seasonal Employer work policy and its role in assisting development in Samoa and Tonga* (2015) at 4 as cited in Patrick Smellie “How anti-money-laundering measures can hurt migrant workers” *New Zealand Listener* (online ed, Auckland, 22 July 2016).

26 “Tonga most dependent in Pacific on remittances” (9 September 2016) Radio New Zealand <www.radionz.co.nz>.

27 See The Treasury, above n 12, at Annex 1. *New Zealand dollar* and *foreign exchange* are abbreviated to NZD and FX respectively.

Money Remitters

Money remitters, also referred to as *money transfer operators* (MTOs), provide services to remit funds instantaneously to rural areas underserved by banks without requiring customers to have bank accounts.²⁸ Money remitters may provide better access than banks, through agents operating from small shops outside central business districts.²⁹ They are also within the definition of a *money service business* (MSB), which is a “non-bank entity providing mechanisms for people to make payments or to obtain currency or cash in exchange for payment instruments by any means through a financial agency or institution”.³⁰ Remittances through money remitters usually amount to USD 5,000 or less as greater amounts are normally remitted through banks.³¹

As shown in Figure 3, money remitters require banking relationships to operate as they receive and transfer funds through their bank account. There are two types of money remitters: traditional remittance systems supervised by the DIA; and alternative or informal value transfer systems, which operate outside the regulated financial channels.³²

In the DIA’s 2011 sector risk assessment, money remitters were reported as having a high overall risk. The DIA noted that money remitters handled high volumes of transactions that are mostly cash-intensive and international, with transactions that can involve high-risk customers in countries with poor AML/CFT measures.³³ Even if a money remitter complies with the AML/CFT Act’s requirements, transactions are perceived as risky if the recipient country does not have adequate AML/CFT regimes.³⁴ Money remitters often pool funds from multiple individual transactions and deposit the resulting fund in a lump sum, which obscures the original sources of the funds.³⁵ This increases the risk of money remitters facilitating terrorist financing. It does so by.³⁶

... performing relevant transactions without knowledge of the illegal origin or destination of the funds concerned or by a direct involvement of the staff/management of the provider through complicity or takeover of such businesses by the criminal organisation.

28 Davis and Jenkinson, above n 16, at 1.

29 Deloitte, above n 24, at [4.4].

30 Kristin Pullar “Blanket De-Risking of Money Service Businesses” (Association of Certified Anti-Money Laundering Specialists, 2016) at 2.

31 Davis and Jenkinson, above n 16, at 1.

32 Department of Internal Affairs *Internal Affairs AML/CFT Sector Risk Assessment* (March 2011) at [97] and n 10.

33 At [96]–[110].

34 Tracey Durner and Liat Shetret *Understanding Bank De-risking and its Effects on Financial Inclusion: An exploratory study* (Global Center on Cooperative Security, November 2015) at 8.

35 At 8.

36 Financial Action Task Force *Money Laundering through Money Remittance and Currency Exchange Providers* (June 2010) at [59].

These features have rendered the use of money remitters a common method of financing terrorist groups, as innocent transfers by migrant families create difficulties in detecting terrorist financing.³⁷

Banks

Banks in New Zealand are registered under the Reserve Bank of New Zealand Act 1989 (RBNZ Act) and are supervised by the RBNZ. Almost all of the 24 registered banks, including the five major banks,³⁸ offer international funds transfer services.³⁹ Banks generally require the sender and recipient to have a bank account, with the sender having an account at the sending bank. The transfer to the overseas bank branch typically takes longer compared to money remitters, as funds cannot be collected until the inter-bank transfer has been completed.

Banks also have unserved or under-served areas where customers who require end-to-end service are unable to access banking services.⁴⁰ Recipients may also face difficulties meeting customer identification requirements when opening bank accounts.⁴¹ As a result, although account-to-account transfers are safer due to stringent AML/CFT processes, they are often unsuitable for low value and high volume remittances, which are often undertaken by foreign workers using money remitters.⁴² Banks also provide banking services to money remitters. Where there is a banking relationship between a bank and a money remitter, the bank performs customer due diligence on money remitters and money remitters provide information relating to transactions, as required by the bank.

Banks generally have a high risk of facilitating terrorist funding as they are well-positioned in the international financial system to transfer funds. The size of the international financial sector allows small-scale terrorist funding to blend in to the large volume and number of legitimate transactions.⁴³ Traditional bank products such as a savings account can be exploited for terrorist financing, for example by enabling a terrorist organisation to withdraw cash from the account through debit cards and ATMs.⁴⁴ In the RBNZ's 2017 sector risk assessment, banks received an overall high risk rating, due to the large number of customers, high number and value of transactions, complex products and business models, and exposure to international financial systems.⁴⁵ The assessment noted that:⁴⁶

37 Financial Action Task Force, above n 1, at 22.

38 The five major banks are ANZ, ASB, BNZ, Kiwibank and Westpac.

39 "List of registered banks in New Zealand — past and present" (30 September 2016) Reserve Bank of New Zealand <www.rbnz.govt.nz>

40 Davis and Jenkinson, above n 16, at 1.

41 Deloitte, above n 24, at [4.8].

42 At [4.8].

43 Financial Action Task Force, above n 1, at 21.

44 At 1.

45 Reserve Bank of New Zealand *Anti-Money Laundering and Countering Financing of Terrorism (AML/CFT): Sector Risk Assessment for Registered Banks, Non-Bank Deposit Takers and Life Insurers* (April 2017) at [57]–[59].

46 At [60].

... for the year to 30 June 2016 over four billion transactions were handled by NZ registered banks, representing over 95% of all transactions in the sector. The banks handled fund movements valued in excess of NZD\$83 trillion, representing approximately 99% of the total funds handled across the sector.

Banks offer a wide range of products, including cash intensive products, to a range of customers including politically exposed persons and high value dealers, while facilitating international transactions, which can include higher risk countries with inadequate or no AML/CFT measures.⁴⁷

Government

The New Zealand government has a policy interest in lowering the cost of remittances to the Pacific. Government actions in the past have included forming an inter-governmental working group to identify and support opportunities to lower remittance costs in the Pacific. New Zealand has also committed to Group of Twenty's (G20) Call to Action on Remittances as a G20 guest country in 2014. The government is working with the banking sector to improve the bankability of small MTOs and to develop low-cost products for seasonal migrant workers. It has also supported initiatives, such as price comparison websites and seasonal worker financial literacy training. New Zealand is also working with global forums, partner governments and agencies in the Pacific to explore ways of reducing the cost of remittances, for instance, by introducing electronic payments systems.⁴⁸

Furthermore, the Treasury in April 2016 awarded a tender for a review of the money remittance market in New Zealand. It asked for the review to:⁴⁹

Firstly, to identify problems affecting cost and access to remittance services between NZ and the Pacific including understanding the drivers of bank account closures in New Zealand, with reference to existing work already completed. Secondly, to develop a set of feasible policy options to address the issues in the New Zealand remittance market that would maintain access and reduce costs of remitting money from NZ to the Pacific.

This is indicative of the government's interest in the availability and cost of money remittance services.

47 At [64]–[69].

48 "G20 Plan to Facilitate Remittance Flows" (20 November 2014) G20 Information Centre <www.g20.utoronto.ca> at 9.

49 "Review of the Money Remittance Market in New Zealand" (17 February 2016) New Zealand Government Electronic Tenders Service <www.gets.govt.nz>. The resulting review prepared by Deloitte was released by the Treasury in March 2017. See generally Deloitte, above n 24.

III THE ISSUE: CLOSURE OF MONEY REMITTERS AND BLANKET DE-RISKING POLICIES

An unintended consequence arising from the AML/CFT regime is the adoption of blanket de-risking policies by banks in New Zealand and abroad, where banks indiscriminately refuse to provide banking services to money remitters. As a result, money remitters are unable to access bank accounts to conduct their business and may be forced to cease their business. This issue features in the United Kingdom High Court case of *Dahabshiil Transfer Services Limited v Barclays Bank plc*⁵⁰ and the recent New Zealand High Court decision of *E-Trans*.⁵¹

Dahabshiil

In *Dahabshiil* a money remitter argued that its bank's decision to close its account was an abuse of market power contrary to competition laws. The case was significant because *Dahabshiil* was the leading remittance broker in the Horn of Africa — including Somalia, a country that lacks a formal banking system and relies solely on MSBs to receive money.⁵² In response to the AML/CFT regime, Barclays terminated *Dahabshiil*'s account. This was even though *Dahabshiil*'s AML/CFT programme satisfied the relevant international regulatory standards and was subjected to regular AML/CFT audits by HM Revenue & Customs, as well as annual or six-monthly audits by Barclays.⁵³

Henderson J recognised that Barclays had a right to choose its customers and that there was no public law duty on banks to make services available to certain classes of customers — despite being heavily regulated entities due to the public interest.⁵⁴ Although the interim injunctions to continue banking services were granted, the parties settled. As a result of the settlement, *Dahabshiil* ended its banking relationship with Barclays and made “alternative arrangements”.⁵⁵

E-Trans

E-Trans is a 2016 New Zealand High Court decision that found a bank acted legally in adopting a blanket de-risking policy and terminating the bank account of a money remitter.⁵⁶ *E-Trans*, a money remitter, had initially conducted its currency exchange and money remittance business through ANZ, ASB and Westpac, before each of those banks adopted policies of

50 *Dahabshiil Transfer Services Ltd v Barclays Bank plc* [2013] EWHC 3379 (Ch).

51 *E-Trans*, above n 4.

52 *Dahabshiil*, above n 50, at [28].

53 At [29].

54 At [2].

55 Max Colchester “Barclays Settles Dispute with Money Transfer Company *Dahabshiil*” *The Wall Street Journal* (online ed, New York, 16 April 2014).

56 *E-Trans*, above n 4.

refusing banking services to money remitters. E-Trans then opened a business account with Kiwibank, which subsequently made a policy decision to terminate its contracts with money remitters. Kiwibank terminated the E-Trans contract in 2015. This was despite E-Trans's application for review and its willingness to comply with any conditions or maintenance fees to mitigate the risks and costs of AML/CFT monitoring.

E-Trans sought a permanent injunction prohibiting Kiwibank from closing its accounts so long as it observed its contractual obligations to Kiwibank. It also sought a declaration that Kiwibank was in breach of its obligations under the AML/CFT Act and the RBNZ Act, and that Kiwibank was not entitled to avoid those obligations by closing the accounts of E-Trans. Heath J found that Kiwibank acted legally in closing E-Trans's account, but also called for legislative action as the policy choices underlying this issue were non-justiciable.

The Minister of Finance at the time, the Hon Bill English MP, declined to make any changes to the AML/CFT Act following *E-Trans*.⁵⁷ As a result, in the absence of any legislative intervention, the precedent set by *E-Trans* allows banks to continue their blanket de-risking policies against money remitters, effectively leading to closures of money remitters.

Regulators' Response

The responses of FATF and regulators in New Zealand and abroad have been to discourage the use of blanket de-risking policies against money remitters and to encourage the use of individualised risk assessment.

The RBNZ has issued an official statement regarding closures of money remitters' bank accounts. It acknowledges money remitters' loss of access to banking services and reiterates that the AML/CFT Act does not require banks to take a "broad-brush approach" in de-risking by closing or refusing to open accounts for an entire category of customers.⁵⁸ It notes that banks' systems and controls should be able to mitigate and manage such risks without resorting to de-risking policies. It also notes that such policies are inadequate to manage the risks of money laundering and terrorist financing. The RBNZ reiterated this message in its 2017 sector risk assessment, where it recognised the risks posed by MSBs, including money remitters, and emphasised that responses to the risks should be proportionate and reflect a risk-based assessment.⁵⁹

Similarly, the FATF noted that money remitters are reliant on access to banking services to operate and that banks should not resort to "wholesale termination or exclusion of customer relationships" without a risk assessment under the risk-based approach.⁶⁰ The risk assessment should

57 Jenée Tibshraeny "Bill English rules out 'radical' policy changes to shield money remitters from banks' blanket de-risking policies" (10 June 2016) interest.co.nz <www.interest.co.nz>.

58 Reserve Bank of New Zealand "Statement about banks closing accounts of money remitters" (media statement, 28 January 2015) <www.rbnz.govt.nz>

59 Reserve Bank of New Zealand, above n 45, at [126].

60 Financial Action Task Force *Guidance for a Risk-Based Approach: Money or Value Transfer Services* (February 2016) at [126].

assess whether the money remitter's particular level of risk can be mitigated. And the level and frequency of monitoring for suspicious transactions should reflect the level of risk, determined from factors such as the:⁶¹

- Products and services offered;
- Types of customers;
- Distribution channels;
- Jurisdictions it is exposed to;
- Experience of the money remitter;
- Purpose of the account;
- Anticipated account activity;
- Scope of markets served, domestic or international;
- Effectiveness of regulatory oversight in the countries of operation; and
- Effectiveness of the money remitter customer's risk management and compliance programs.

Furthermore, banks should conduct a risk-based review of transactions to “detect any significant unexplained variations in transaction size, nature or frequency through the account which could reveal potentially suspicious operations”.⁶²

The Financial Conduct Authority (FCA) in the United Kingdom also issued an official statement which addresses de-risking policies affecting money remitters. It clarifies that banks are expected to take a risk-based approach and that it will consider consumer protection and competition issues when faced with de-risking policies.⁶³

Finally, in the United States the Financial Crimes Enforcement Network (FinCEN) is responsible for enforcing the Bank Secrecy Act 1970, while a number of agencies are responsible for administering the AML/CFT requirements. FinCEN issued an official statement of its expectations on banks not to indiscriminately terminate accounts of MSBs, including money remitters. It urged banks to evaluate MSB accounts on a case-by-case basis, as not all MSBs are high-risk.⁶⁴ It also clarified that banks were only required to understand the MSB customer's business model and customer base, and were not required to know whether they comply with the Bank Secrecy Act.⁶⁵

These public statements by various regulators show that the use of blanket de-risking policies is a serious concern and that such policies are not intended by the AML/CFT regime, which prefers a risk-based approach.

61 At [127]–[128].

62 At [133].

63 “De-risking: managing money-laundering risk” (20 May 2016) Financial Conduct Authority <www.fca.org.uk>.

64 United States Department of the Treasury Financial Crimes Enforcement Network “FinCEN Statement on Providing Banking Services to Money Services Businesses” (10 November 2014) <www.fincen.gov> at 2.

65 At 3.

IV CAUSES AND MOTIVATIONS OF BLANKET DE-RISKING POLICIES

Recent closures of money remitters have contributed towards an increase in the price of remittances.⁶⁶ These changes have been attributed to money laundering and terrorist financing risks, and “compliance costs to effectively mitigate those risks, profitability, reputational risk and requirements imposed by international correspondent banks”.⁶⁷

The AML/CFT requirements have increased the costs of providing banking services to money remitter customers due to the intensive due diligence and monitoring associated with high-risk customers. As banks are businesses with a profit incentive, the closures of money remitters’ accounts suggest that retaining them entails high compliance costs, which in turn results in low profitability. The strength of this profit incentive is highlighted in the Financial Services Authority’s 2011 survey of 27 United Kingdom banking groups which found that some banks were willing to maintain unacceptable risks of handling proceeds of crime if the relationships were profitable.⁶⁸ Moreover, around a third of the banks appeared willing to maintain a high risk “if the immediate reputational and regulatory risk was acceptable”.⁶⁹

This is evident in *Dahabshil*, where Barclays created minimum standards setting out the criteria for retaining MSB customers.⁷⁰ For example, it required a minimum of £10 million of net tangible assets, a high level that eliminated many money remitters and deemed only those representing more than £100,000 in annual revenue as commercially viable.⁷¹ Barclays’ MSB Approval Committee also retained an “overriding discretion” to approve or reject customers, regardless of the level of compliance with the minimum standards.⁷² As a result, only 19 out of a total of 165 money remitters were retained as customers, amounting to a reduction of 88 per cent.⁷³

Banks incur substantial costs in developing and maintaining systems to comply with the AML/CFT Act. In New Zealand, banks must appoint an AML/CFT compliance officer and maintain a compliance programme that encompasses:⁷⁴

- ... vetting and training certain staff

66 The Treasury, above n 12, at [11].

67 Financial Action Task Force, above n 60, at [135].

68 Financial Services Authority *Banks’ management of high money-laundering risk situations: How banks deal with high-risk customers (including politically exposed persons), correspondent banking relationships and wire transfers* (June 2011) at [7].

69 At [7].

70 *Dahabshil*, above n 50, at [22].

71 At [22].

72 At [24].

73 At [25].

74 “What are reporting entities required to do?” Reserve Bank of New Zealand <www.rbnz.govt.nz>.

- carrying out due diligence on customers (CDD) (which includes customer identification and verification)
- undertaking ongoing customer due diligence and account monitoring
- reporting suspicious transactions
- record-keeping
- monitoring and management of AML/CFT matters in an ongoing way ...

Furthermore, if a bank has reasonable grounds to suspect transactions may be relevant to enforcement of, among other things, the Terrorism Suppression Act 2002, they must report the transactions to the Police Commissioner as soon as practicable and no later than three working days after first forming suspicion.⁷⁵ Experience from banks in the United States, the United Kingdom and Spain has shown that, even with investment in software to monitor transactions, banks need to manually investigate any suspicious activities.⁷⁶ Indeed, money remitters frequently transact small amounts across jurisdictions and this leads to a complex operational and compliance burden, which is not offset by the volume of transactions.⁷⁷

Obligations to report suspicious transactions open banks up to financial and reputational risks. If banks fail to report a suspicious transaction they may face criminal and civil sanctions. These sanctions include a fine of up to NZD 5 million for the company; and a fine of up to NZD 300,000 and up to two years' imprisonment for individuals who are employees or officers of the company.⁷⁸ AML/CFT fines have led to a more risk-averse behaviour and often zero tolerance to all money laundering and terrorist financing risks.⁷⁹ This is despite the fact that fines have been levied only for serious failures in a bank's controls rather than for failures in the bank's customer.⁸⁰ In addition to the financial risk, reputational risk can arise from the adverse publicity associated with legal proceedings, where the general public may regard defendant banks as being complicit in money laundering and terrorist financing.⁸¹ These risks may also be heightened due to a rise in AML/CFT enforcement actions after the 2008 Global Financial Crisis. In these actions regulators sought to punish banks that were not perceived to be held sufficiently accountable for their role in the crisis.⁸² Also, banks face a high risk of inadvertently facilitating terrorist

75 Anti-Money Laundering and Countering Financing of Terrorism Act 2009, s 40.

76 Michael Corkery "Immigrants From Latin America and Africa Squeezed as Banks Curtail International Money Transfers" *The New York Times* (online ed, New York, 6 July 2014).

77 Durner and Shetret, above n 34, at 10.

78 Section 100.

79 David Artingstall and others *Drivers & Impacts of Derisking: A study of representative views and data in the UK*, by John Howell & Co Ltd for the Financial Conduct Authority (John Howell & Co, Surrey, 2016) at 71.

80 At 71.

81 *E-Trans*, above n 4, at [146]–[148].

82 Durner and Shetret, above n 34, at 8.

financing and money laundering due to the nature of their business. Therefore, banks may be unwilling to further increase the risks and expenses related to AML/CFT compliance by retaining high-risk customers.

It should also be noted that these risks become concentrated on fewer banks as more banks adopt blanket de-risking policies. In *Dahabshil*, HSBC's USD 1.9 billion settlement of cases with the United States authorities involving AML/CFT controls triggered its withdrawal of banking services to MSBs, including money remitters. The withdrawal prompted MSBs to move banks, which led to an increase in the number of MSBs wishing to bank with Barclays.⁸³ This resulted in a concentration of high-risk customers at Barclays, raising the level of potential risks it faced.⁸⁴

In *E-Trans*, Kiwibank was the last major bank to adopt a blanket de-risking policy and was described as the "bank of choice" for money remitters.⁸⁵ Banks without blanket de-risking policies become burdened with a higher concentration of risk, and so banks have become incentivised to adopt them.

Closures of money remitters' bank accounts can also be attributed to AML/CFT regulations in other jurisdictions, particularly the United States, through correspondent banks.⁸⁶ Correspondent banks provide financial services, such as fund transfers to banks. New Zealand and Australian banks may have banking relationships with United States-based correspondent banks, to access their financial system and currency — the most commonly-used currency for international transfers.⁸⁷ As a result, New Zealand is indirectly exposed to the United States' regulations. In the United States, all international remittances are classed as high-risk, regardless of the destination or amounts involved,⁸⁸ and United States banks "can be held liable for the AML/CTF compliance failure of any foreign bank whose funds they clear".⁸⁹ Therefore, New Zealand and Australian banking groups have experienced pressure from correspondent banks in the United States to cease or limit services to money remitters, with a possibility of losing access to their United States currency clearing facilities for failing to do so.⁹⁰ Similarly, Australian banking groups face a risk of having their United States bank licence revoked.⁹¹ Globally, 75 per cent of 20 large international banks reported a decline in correspondent banking relationships from 2012 to mid-2015.⁹²

83 *Dahabshil*, above n 50, at [17]–[18].

84 At [18].

85 *E-Trans*, above n 4, at [50].

86 The Treasury, above n 12, at [13]–[19].

87 At [20].

88 At [21].

89 USA PATRIOT Act of 2001 Pub L No 107-56, §312, 115 Stat 272 at 304 as cited in Rebecca L Stanley and Ross P Buckley "Protecting the West, Excluding the Rest: The Impact of the AML/CTF Regime on Financial Inclusion in the Pacific and Potential Responses" (2016) 17 Melbourne Journal of International Law 83 at 99.

90 See The Treasury, above n 12, at [22].

91 At [22].

92 World Bank Group *Withdrawal from Correspondent Banking: Where, Why, and What to Do About it* (Working Paper 101098, November 2015) at [10]–[12].

These factors drive the banks' exercise of their freedom as private businesses to choose their customers. Both *E-Trans* and *Dahabshiil* recognised that banks are not under a public law duty to make services available to particular classes of customers. In *E-Trans*, Kiwibank sought to protect its ability to determine the risks of dealing with certain categories of customers and decide whether maintaining a customer relationship was justified.⁹³ These determinations are especially important for banks in the context of AML/CFT compliance, where the cost of complying with the AML/CFT Act's requirements increases with the customer's riskiness. The money remitters' inherently risky characteristics mean that banks face a higher cost in monitoring them in compliance with the AML/CFT Act, as they seek to avoid the realisation of financial and reputational risks.

However, it is worth noting that the closure of money remitters may also be attributed to factors beyond blanket de-risking policies. The AML/CFT regime imposes high compliance costs which are fixed. As a result, the regime tends to affect "small-scale, localized and personalized" money remitters disproportionately compared to international corporations.⁹⁴

FATF considers de-risking to be a complex issue that "goes far beyond" AML/CFT.⁹⁵ Therefore, more evidence is needed to determine its causes, scale and impact.⁹⁶ The International Monetary Fund has also attributed the withdrawal from correspondent banking relationships, which is an aspect of de-risking, to other regulatory requirements such as trade sanctions, prudential requirements, cross-border legal obstacles to compliance and tax transparency.⁹⁷

V CONSEQUENCES OF BLANKET DE-RISKING POLICIES

Blanket de-risking policies prevent money remitters from obtaining bank accounts. As remittances are conducted through bank accounts, money remitters are likely to first shift to banks without de-risking policies. Those institutions might be smaller banks and credit unions without adequate systems for higher-risk customers.⁹⁸ They might also adopt de-risking policies in response to higher risks, as seen in *E-Trans* and *Dahabshiil*. Money remitters may be driven out of business. If this was to happen, an individual seeking to remit money would face the alternative options of remitting through a bank, not remitting, or remitting through informal channels. These options diminish the benefits of remittances and increase

93 At [149].

94 Cooper and Walker, above n 5, at 1130.

95 "Drivers for 'de-risking' go beyond anti-money laundering / terrorist financing" (26 June 2015) Financial Action Task Force <www.fatf-gafi.org>.

96 "Drivers for 'de-risking' go beyond anti-money laundering / terrorist financing".

97 Michaela Erbenová and others *The Withdrawal of Corresponding Banking Relationships: A Case for Policy Action* (International Monetary Fund, Staff Discussion Note SDN/16/06, June 2016) at [13].

98 Durner and Shetret, above n 34, at 19.

costs for customers, while creating a higher risk of terrorist financing by proliferating unmonitored informal channels.

Higher Prices

Closures of money remitters are likely to lead to increases in the prices of remittances because money remitters enable cheaper remittances compared to banks. According to SendMoneyPacific, an independent cost comparison website for money transfers, a transfer of NZD 200 from New Zealand to Samoa via a bank costs an average of 15.96 per cent compared to an average of 8.27 per cent for money remitters.⁹⁹ This difference can be attributed to money remitters' specialised business model and infrastructure, which lower their costs by aggregating funds for transfer.¹⁰⁰

As banks compete with money remitters in providing remittance services, banks may close money remitters' accounts to eliminate competition in the remittance market.¹⁰¹ In Samoa, money remitters handled at least 80 per cent of remittance inflows, but by the end of March 2015, all major Australian commercial banks had closed bank accounts of most money remitters linked to Samoa.¹⁰² Furthermore, there was a 50 to 60 per cent decrease in the number of money remitters when two major banks in Australia — the Commonwealth Bank and the National Australia Bank — adopted blanket de-risking policies against money remitters.¹⁰³ And in New Zealand, there was a decrease of almost 20 per cent in the number of money remitters between 2011¹⁰⁴ and 2016.¹⁰⁵ Allowing banks to indiscriminately refuse banking services to money remitters through their blanket de-risking policy is likely to lead to an elimination of money remitters from the remittance market, resulting in diminished competition with banks being the sole providers of remittance services.

Diminished competition in the remittance market would increase the price of remittance services. An examination of remittances in 119 country pairs found that lower competition, and a higher share of banks among providers, were correlated with higher prices of remittances.¹⁰⁶ In Australia,

99 "Comparison Results" (19 October 2017) SendMoneyPacific <www.sendmoneypacific.org>. This fluid data is correct at the time of printing.

100 Ole Andreassen *Remittance Service Providers in the United States: How remittance firms operate and how they perceive their business environment* (World Bank, Financial Sector Discussion Report No 37600, June 2006) at 2 as cited in Davis and Jenkinson, above n 16, at 11.

101 See for example Sonia Plaza "Closing of bank accounts of money transfer operators (MTOs) is raising remittance costs" (22 October 2014) People Move <www.blogs.worldbank.org>.

102 Atalina Ainuu-Enari, Governor of the Central Bank of Samoa "Intervention by the Governor of the Central Bank of Samoa, Atalina Ainuu-Enari" (speech to the Commonwealth Central Bank Governors Meeting, Lima, Peru, 6 October 2015).

103 Pacific Islands Forum Secretariat "Financial Infrastructure and Fiscal Space: Access to Finance and Financial Infrastructure" (July 2014) <www.forumsec.org> at [4].

104 "Department of Internal Affairs AML/CFT Reporting Entities as at 1 May 2011" (1 May 2011) Department of Internal Affairs <www.dia.govt.nz>.

105 "Department of Internal Affairs AML/CFT Reporting Entities as at 30 June 2016" (30 June 2016) Department of Internal Affairs <www.dia.govt.nz>.

106 Thorsten Beck and María Soledad Martínez Peria "What Explains the Price of Remittances? An Examination Across 119 Country Corridors" (2011) 25 World Bank Econ Rev 105 at 129.

closures of seven money remitters preceded the increase in average cost of remittances from “8.88 per cent in the third quarter of 2014, to 9.24 per cent in the third quarter of 2015”.¹⁰⁷ In comparison, during the same period, the global average cost fell from 7.9 per cent to 7.52 per cent.¹⁰⁸ In 2016, five out of ten Pacific countries reported that inbound remittances became more costly and burdensome, with Tonga and Fiji specifying that the cost of remittances from New Zealand had risen.¹⁰⁹ This is supported by the Remittances Prices Worldwide database, which suggests an increasing trend in remittance cost over the past three years in New Zealand.¹¹⁰

Average Total Costs of Remitting NZD 260 to Samoa 2013–2016

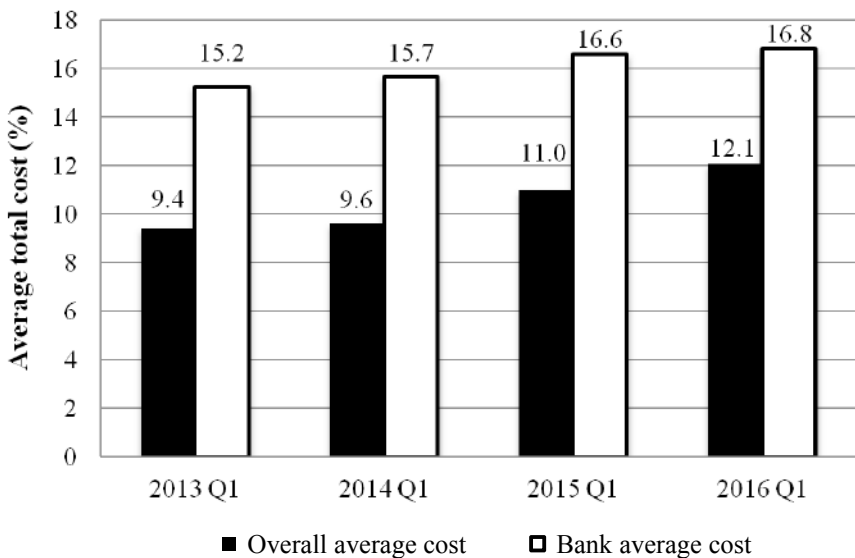


Figure 5: Average Total Costs of Remitting NZD 260 to Samoa 2013–2016

If customers are willing and able to pay this higher price, the resulting change may be negligible. But this is unlikely if customers are unwilling or unable to pay the price. The latter scenario may be more plausible as the higher price combined with banks’ lack of remittance services to rural areas and customers without bank accounts may discourage remittances through the traditional and regulated channels (represented by banks).

107 World Bank *Remittance Prices Worldwide* (No 15, October 2015) as cited in Stanley and Buckley, above n 89, at 92.

108 At 92.

109 Jihad Alwazir and others *Challenges in Correspondent Banking in the Small States of the Pacific* (International Monetary Fund Working Paper WP/17/90, April 2017) at 8.

110 “Sending money from New Zealand to Samoa” (16 February 2016) Remittance Prices Worldwide <www.remittanceprices.worldbank.org>.

Impact on Economic and Social Development

If remittances were discouraged due to their high cost and limited accessibility, this could diminish or eliminate the positive effects of remittance flows in recipient countries and negatively impact economic and social development.¹¹¹ Remittances can alleviate poverty by paying for basic needs, such as food, shelter and healthcare,¹¹² while creating a stronger demand for financial products.¹¹³ This can help to develop a country's financial sectors. For instance, remittance receipts can be used to judge the creditworthiness of poorer individuals and improve their financial inclusion.¹¹⁴ It can also fund investments in human capital, such as education, entrepreneurship and health.¹¹⁵ Remittances have wide geographic dispersion and can stimulate economic development, especially in rural developing areas.¹¹⁶ Because remittance flows tend to increase during times of need, they can also play an important role as a form of insurance during times of conflict, political instability or natural disasters.¹¹⁷ Remittances also support the economic empowerment of women — approximately two thirds of recipients globally are women — by helping to facilitate women to start their own businesses with the accumulated capital.¹¹⁸ Unlike aid money, remittances have a direct impact on the poor as they are sent directly to the people and communities who need them most, rather than through governments and officials.¹¹⁹ This is especially the case for the rural poor in developing countries where opening and maintaining bank branches in remote locations requires significant transaction costs — which are not usually offset by profits.¹²⁰

The effects of remittances are relevant to the New Zealand government's objective of "increasing prosperity in the Pacific".¹²¹ The Pacific is "one of the least banked regions in the world", with less than 10 per cent of the population having access to basic financial services.¹²² It is also prone to natural disasters, with many people depending on family members when shocks occur.¹²³

111 See G20 Information Centre, above n 48, at 2–3.

112 Stanley and Buckley, above n 89, at 88.

113 G20 Information Centre, above n 48, at 3.

114 Dilip Ratha and others *Migration and Remittances: Recent Developments and Outlook Special Topic: Financing for Development* (World Bank, Migration and Development Brief No 24, 13 April 2015) at [3.6].

115 Stanley and Buckley, above n 89, at 86–87.

116 G20 Information Centre, above n 48, at 3.

117 Dilip Ratha and others, above n 114, at [1.3].

118 G20 Information Centre, above n 48, at 3.

119 L Le De and others "Remittances in the face of disasters: a case study of rural Samoa" (2015) 17 *Environ Dev Sustain* at 653 and 659 as cited in Stanley and Buckley, above n 89, at 89.

120 Durner and Shetret, above n 34, at 21.

121 Letter from Bill English (Minister of Finance) to Paul Brock (Chief Executive of Kiwibank) regarding remittances to the Pacific (16 December 2015) as cited in *E-Trans*, above n 4, at [82].

122 Pacific Financial Inclusion Programme "Achieving Financial Inclusion in the Pacific" <www.pfip.org> as cited in Stanley and Buckley, above n 89, at 90.

123 Ken C Ooi and Ross P Buckley "Pacific Injustice and Instability: Bank Account Closures of Australian Money Transfer Operators" (2014) 25 *JBFLP* 243 at 244.

Closures of money remitters may have a negative societal and economic impact on communities that rely on remittances. If individuals choose to pay a higher price for remittances, remittances have a diminished effect on alleviating poverty as a greater proportion of intended remittance funds are paid to financial intermediaries.¹²⁴ If individuals choose not to remit — or are unable to remit — to unbanked communities, those communities may become more susceptible to predatory private lenders with links to extortion and threats of violence.¹²⁵ These lenders can impose staggering fees and extraordinarily high interest rates without customer protection.¹²⁶ Counterterrorism measures may be undermined through local terrorist groups filling the vacuum left by remittances to obtain support,¹²⁷ and frustrations caused by the inability to remit funds could increase the risk of people being radicalised.¹²⁸ Therefore, a lack of access to remittances may increase the community's vulnerability to costlier and less-regulated services.

Some commentators argue that de-risking policies could sever vulnerable communities' access to financial services and that this would result in financial exclusion, with implications for human rights violations.¹²⁹ Limiting or severing access to remittances in underdeveloped financial systems could then compel income-generating activities that put human rights at risk. For example, the use of child labour tends to increase when households experience a negative shock to income or restricted access to credit, especially in countries with underdeveloped financial sectors.¹³⁰ Financial exclusion may also have implications for domestic violence, which has been found to increase with financial exclusion.¹³¹

Proliferation of Informal Channels

Informal channels, also called alternative remittance systems, involve moving funds from one site to another through a personal network, usually with ties to a particular geographical location.¹³² An example is the *hawala* system, which is an honour-based system used predominantly in the Middle East, Asia and some parts of Africa.¹³³ It works on trust and reliable

124 Stanley and Buckley, above n 89, at 89.

125 Apanard (Penny) Prabha and Minoli Ratnatunga "Underground Lending: Submerging Emerging Asia?" (April 2014) Milken Institute <www.assets1b.milkeninstitute.org> at 9.

126 Durner and Shetret, above n 34, at 5.

127 Aimen Dean, Edwina Thompson and Tom Keatinge "Draining the Ocean to Catch one Type of Fish: Evaluating the Effectiveness of the Global Counter-Terrorism Financing Regime" (2013) 7(4) Perspectives on Terrorism 62 at 70.

128 At 70.

129 Durner and Shetret, above n 34, at 22.

130 Kathleen Beegle, Rajeev Dehejia and Roberta Gatti "Child Labor, Crop Shocks, and Credit Constraints" (November 2003) National Bureau of Economic Research <www.nber.org> at 2.

131 See Durner and Shetret, above n 34, at 23.

132 Cooper and Walker, above n 5, at 1125.

133 Charles B Bowers "Hawala, Money Laundering, and Terrorism Finance: Micro-Lending as an End to Illicit Remittance" (2009) 37 Denv J Intl L & Poly 379 at 379–380.

connections. The *dealer* receives the money from the *sender* and contacts its *correspondent* in the country the money is being sent to, who then arranges for the equivalent money in the local currency to be delivered to the *recipient*.¹³⁴

While such alternative remittance systems are cheaper and more efficient, there is usually no audit trail or documentary proof of the transfer.¹³⁵ Senders and recipients are not required to have any official documentation or bank account, and dealers are not subject to supervision by authorities. The reciprocal trust underpinning the system may arise from shared ethnicity, religion, social standing, or business connections.¹³⁶ Because of reciprocal trust there is no close scrutiny of the transaction's purpose, the source of the funds or the identities of the sender and recipient.¹³⁷ As a result, the *hawala* system allows "inexpensive, anonymous and virtually non-traceable transactions"¹³⁸ outside the regulated financial sector, with no consumer protection and high risks of terrorist financing. According to FATF, these features have led to the creation of alternative remittance systems for the purpose of terrorist financing.¹³⁹ Although such systems use the banking system when handling large amounts of cash, the systems' indirect fund movements and trust-based nature¹⁴⁰ make it difficult to obtain intelligence showing direct terrorist financing links.¹⁴¹

If money remitters were to be driven out of business, there may be a proliferation of alternative remittance systems. This is because senders seek out alternative avenues to remit money cheaply or to remote areas without banking services. These alternative avenues may in turn lead to a loss of transparency and greater terrorist financing risks, as they are unregulated, unsupervised and difficult to trace. Moreover, even if transfers through informal money remitters can be investigated, the greater volume of innocent transfers creates difficulties in the detection of terrorist financing as illegitimate transfers are drowned out by legitimate transfers, resulting in an enhanced risk of terrorism financing. Finally, this undermines the aim of the AML/CFT regime, which is to detect and deter financing of terrorism.

134 Arvinder Sambei, Anton du Plessis and Martin Polaine *Counter-Terrorism Law and Practice: An International Handbook* (Oxford University Press, New York, 2009) at [7.10].

135 At [7.10].

136 Cooper and Walker, above n 5, at 1128.

137 At 1128.

138 Sambei, du Plessis and Polaine, above n 134, at [7.13].

139 See Financial Action Task Force *Report on Money Laundering Typologies 2002–2003* (Paris, 2003) at [23]–[24].

140 Financial Action Task Force, above n 36, at [82].

141 Financial Action Task Force, above n 139, at [23].

VI POSSIBLE SOLUTIONS

In light of the *E-Trans* decision, Mr English has commented that it would be difficult for the government to enact legislation that counters the “careful, conservative environment” put in place by the AML/CFT Act.¹⁴² The government is also undertaking work to lower the cost of remittances to the Pacific. In this section I consider arguments against intervention and conclude that intervention is preferable. I then argue for government intervention as the preferred solution.

No Intervention

1 Maintaining Reputation

One of the reasons cited by Mr English is that maintaining New Zealand’s international reputation entails adopting regulations from FATF and bearing the high compliance costs. He argues that the international model does not have room for variations “without creating holes in the system”.¹⁴³ The Treasury also advises that any reforms should “not take New Zealand out of alignment with its international obligations”.¹⁴⁴ Furthermore, New Zealand is scheduled for a mutual evaluation in November 2019,¹⁴⁵ where the FATF evaluates the implementation of FATF recommendations in its member countries and publishes any shortcomings in a report.¹⁴⁶ These shortcomings must then be addressed during post-assessment monitoring.¹⁴⁷ Failure to comply with FATF recommendations may result in a public warning from FATF.¹⁴⁸ It can also affect a country’s reputation, which can lead to the country being excluded from other countries’ *safe* lists, having its credit rating downgraded and experiencing a decline in trade.¹⁴⁹ Indeed, New Zealand was excluded from the European Union’s white list as a result of a 2009 mutual evaluation finding that New Zealand’s implementation of FATF recommendations was inadequate.¹⁵⁰ While this finding predated the AML/CFT Act, it nonetheless led to a more difficult trade situation for New Zealand businesses, as well as New Zealand’s failure to regain entry into the European Union white list, despite the subsequent removal of major deficiencies.¹⁵¹

Although it may be undesirable for AML/CFT reforms to deviate from international obligations, it is also arguable that the issue of blanket de-

142 Tibshraeny, above n 57.

143 Tibshraeny, above n 57.

144 The Treasury, above n 12, at [34].

145 Financial Action Task Force Secretariat *Global Assessments Calendar* (31 July 2015) <www.fatf-gafi.org>.

146 Financial Action Task Force “Mutual Evaluations” <www.fatf-gafi.org>.

147 Financial Action Task Force, above n 146.

148 The Treasury, above n 12, at Annex 2.

149 At Annex 2.

150 At Annex 2.

151 At Annex 2.

risking policies is a global concern. It is a particular concern of the FATF considering the heightened risk of terrorist financing through informal channels and the societal and economic implications of financial exclusion. The extent to which reforms take New Zealand out of alignment depends on the proposed reform, and government intervention may be possible without significant deviations from the FATF recommendations.

2 *Government's Role in the Market*

The government is also reluctant to coerce banks into taking risks they do not want to take. Whether or not this concern is valid, de-risking represents a *market failure* where apparently rational decisions of stakeholders lead to unintended consequences of costly, inaccessible or unmonitored remittances.¹⁵² As a result, de-risking requires government intervention to realign market factors through incentive programs or enhanced regulatory guidance¹⁵³ — for example, by decreasing the risk represented by money remitters through regulatory intervention.

3 *International Response*

The Treasury suggests that any policy changes should include full considerations of international implications,¹⁵⁴ as changes in the international AML/CFT system would have a greater impact in addressing the issue than domestic policies. Domestic policy work requires a resource-intensive cross-agency approach involving the Ministry of Foreign Affairs and Trade, the Ministry of Justice, the Ministry of Business Innovation and Employment, the DIA and the RBNZ.¹⁵⁵ Shifts in the international AML/CFT system would affect the banks' treatment of money remitters through a potential change in pressure from correspondent banks. However, this is only one of the causes of blanket de-risking policies and the prospect of any international change is unclear.¹⁵⁶

4 *Policies in Place to Lower Remittance Costs*

The Treasury noted in May 2015 that there are substantive pieces of work underway — including a response to the World Bank's review of remittance market in New Zealand, and an assessment of the economic impact of Recognised Seasonal Employer remittances in Tonga and Samoa.¹⁵⁷ The government has also invested in a website¹⁵⁸ which compares remittance

152 Durner and Shetret, above n 34, at 3.

153 At 3.

154 The Treasury, above n 12, at [34].

155 At [35].

156 At [37].

157 The Treasury *Briefing: Update on the Cost of Remittances to the Pacific* (20 August 2015) at 3 (Obtained under Official Information Act 1982 Request to the Treasury).

158 SendMoneyPacific "What is SendMoneyPacific?" <www.sendmoneypacific.org>.

prices across *companies, countries and sizes of funds*, and is working with service providers to develop innovative remittance products.¹⁵⁹ It is also contributing to develop modern payments infrastructure in four Pacific islands.¹⁶⁰ This investment in electronic payment systems is expected to reduce the costs of inter-bank transfers and allow mobile telephone companies to transfer money electronically to the Solomon Islands, Samoa, Tonga and Vanuatu.¹⁶¹ However, the use of this technology depends simplifying the implementation of the AML/CFT Act, and these measures only address the remittance costs of specific Pacific countries.¹⁶² Moreover, these measures may not be sufficient for lowering the cost of remittances in the context of blanket de-risking policies as the resulting uncompetitive remittance market removes the banks' incentives to pass on the lower cost of providing remittance services to customers.¹⁶³ Accordingly, the efficacy of these policies in sustainably lowering remittance costs depends on money remitters continuing to operate in the market.

5 *Reliance on Banks and Supervisors*

A solution suggested by Kristin Pullar is for regulators to allow banks to apply their own risk-based approach as an alternative to legislative intervention.¹⁶⁴ She argues that regulators should support banks' evaluations of money remitters' accounts, while improving the oversight of money remitters, given their inherently high-risk business model.¹⁶⁵ This would discourage blanket de-risking policies because banking relationships with money remitters generate revenue for banks.

The Treasury also mentions that it received anecdotal information of banks in New Zealand considering personalised pricing structures for higher risk customers.¹⁶⁶ These pricing structures allow banks to charge money remitters a fee that reflects the costs of taking on the risk, and may result in more money remitters having access to banking services.¹⁶⁷

However, these solutions do not take into account the fact that banks also sell remittance services and compete in the same market as money remitters. This means that banks may have a greater profit incentive in closing money remitters' accounts to capture the money remitters' customers and charge a higher price for remittance services. While more information is required about how much revenue a typical money remitter brings to a New Zealand bank, evidence from Barclays shows that only 19 out of the 165 banking relationships with money remitters were profitable enough to

159 The Treasury, above n 12, at [31].

160 At [31].

161 At [31].

162 Stanley and Buckley, above n 89, at 104.

163 The Treasury, above n 157, at Annex 1.

164 Pullar, above n 30, at 13.

165 At 13.

166 The Treasury, above n 157, at [17].

167 At [17].

retain.¹⁶⁸ This suggests that having a banking relationship with a money remitter is not as profitable or lucrative as Pullar suggests. *E-Trans* demonstrates this as well: *E-Trans*'s offer to Kiwibank to pay a higher price for its banking services to reflect its higher risk and AML/CFT compliance costs was declined, with a blanket de-risking policy being preferred.¹⁶⁹

Pullar's suggestion is similar to a solution proposed by Heath J in *E-Trans*. His Honour suggested that the Minister could exempt banks from the reporting requirements for money remitters and allow the banks to rely on the reporting undertaken by the money remitter.¹⁷⁰ The AML/CFT Act allows a reporting entity to rely on another reporting entity to conduct the required customer due diligence procedures.¹⁷¹ This solution may be appropriate if the underlying rationale is to lower the cost of AML/CFT compliance by relying on another reporting entity.

However, banks are likely to be reluctant to rely on money remitters' customer due diligence because banks remain responsible for ensuring that the customer due diligence complies with the AML/CFT Act's requirements.¹⁷² A 2016 FCA survey of United Kingdom banks found that, despite regulators clarifying that banks do not need to perform due diligence on customers of their customers, they believe they must mitigate the underlying risk themselves if they believe their customer's AML/CFT controls are inadequate.¹⁷³ The risk of relying on money remitters' processes is illustrated by the DIA's filing of civil proceedings against two money remitters for failures to meet the AML/CFT Act's requirements — the first proceedings to be filed since the Act came into effect.¹⁷⁴ In the face of potentially high financial and reputational costs, banks are unlikely to be willing to rely blindly on money remitters' customer due diligence.

Heath J also suggested that the supervisor could provide guidance for banks to assess risks posed by money remitters on a case-by-case basis.¹⁷⁵ This may occur through the RBNZ using its powers under the AML/CFT Act to produce guidelines, prepare codes of practices, provide feedback on compliance and undertake any activities necessary for assisting reporting entities to understand how to achieve compliance.¹⁷⁶ His Honour's suggestion is supported by the FCA's report, which indicates that banks generally preferred more prescriptive guidance on managing high-risk relationships, as well as guidance on what regulators view as acceptable levels of risk.¹⁷⁷

168 *Dahabshil*, above n 50, at [25].

169 *E-Trans*, above n 4, at [63]–[64].

170 At [152].

171 Section 33.

172 Section 33(3).

173 Artinstall and others, above n 79, at 70–71.

174 Department of Internal Affairs "Internal Affairs takes action against two money remitters" (press release, 8 September 2016).

175 *E-Trans*, above n 4, at [152].

176 Section 132(2)(c).

177 Artinstall and others, above n 79, at 70.

This solution would require the RBNZ to go beyond issuing public statements criticising blanket de-risking policies. Similar public statements in the United Kingdom encouraging case-by-case risk assessments have been found to have limited effect on discouraging de-risking policies in banks.¹⁷⁸ Banks surveyed in the United Kingdom either did not believe they were de-risking or believed they were carrying out a case-by-case de-risking aligned with risk-based management of higher risk customers.¹⁷⁹ The RBNZ may be reluctant to act without express clarification of the legislature's stance on blanket de-risking policies or the extent of the powers that the RBNZ may have when faced with blanket de-risking policies. This means that a review or reform of the AML/CFT Act may be required.

Preferred Solution: Government Intervention

There are two options the government might choose for money remitters after the judgment of *E-Trans*: to allow them to close; or to keep them open. If the government wishes to allow money remitters to close, it must address the consequences of blanket de-risking policies. If the government wishes to keep money remitters open it must address the causes of blanket de-risking policies. Immediate steps must also be taken while the government develops these policies, given the societal and economic importance of inexpensive and accessible remittance services.

1 Allow Money Remitters to Close

If the government decides to allow money remitters to close, it should address the consequences of blanket de-risking policies, which includes the higher price of remitting funds, limited access to remittances, and the proliferation of unsupervised informal channels of remittances.

A solution may be to encourage digital financial services (DFS), which enable remittances through mobile phones.¹⁸⁰ DFS can be implemented by banks and mobile network providers and do not require banks to have branches in rural areas.¹⁸¹ In allowing innocent transfers to be remitted relatively cheaply to unbanked areas through regulated banks, DFS may discourage the use of informal channels and decrease terrorist financing risks. DFS also facilitate banks to be compliant with AML/CFT requirements, as remittances are easier to trace in electronic transactions.¹⁸² Figure 6 shows the average cost of remitting NZD 200 from New Zealand to Samoa according to the method of transfer.¹⁸³

178 At 70.

179 At 70.

180 Stanley and Buckley, above n 89, at 102.

181 Ross Buckley and Louise Malady *Digital Financial Services in the Pacific: Experiences and Regulatory Issues* (Asian Development Bank, 2016) at 3.

182 Stanley and Buckley, above n 89, at 103.

183 SendMoneyPacific "Comparison Results" (19 October 2017) <www.sendmoneypacific.org>.

Average Total Cost (%) of Remitting NZD 200 from New Zealand to Samoa

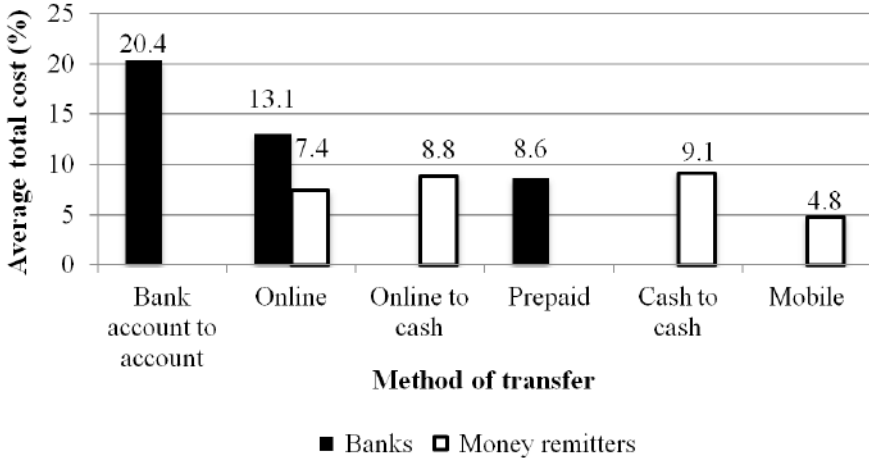


Figure 6: Average Total Cost (%) of Remitting NZD 200 from New Zealand to Samoa (as at 19 October 2017)

The graph shows that transferring funds through mobile phones had the lowest average cost — less than half of bank account to bank account transfers. Also, only one company transferred funds through mobile technology.

The accessibility of DFS depends on the existence of reliable and widely available telecommunications infrastructures, as well as financial competency. Mere access to technology or bank accounts is insufficient to ensure usage if consumer awareness is limited.¹⁸⁴ This means that the New Zealand government may need to intervene to encourage the development and use of DFS for remittances. In addition, the government may need to ensure that the AML/CFT Act addresses the role of telecommunications providers in the AML/CFT regime. This is because DFS allows mobile phone SIM cards to be used for payments. For example, the financial regulator may need to coordinate with the telecommunications regulator to align the AML/CFT requirements of SIM card and bank account registration processes,¹⁸⁵ while simplified regulation for low-value transfers may also facilitate the development of DFS.¹⁸⁶

The government may also encourage banks to create products that lower the cost of remittances through amendments of — or exemptions from — the AML/CFT Act. For example, the cross-government New

184 Buckley and Malady, above n 181, at 2.

185 At 20.

186 Stanley and Buckley, above n 89, at 104.

Zealand-Pacific Remittance Project in 2007 led the government to exempt remittances through electronic cards from the AML/CFT Act through the Financial Transactions Reporting (Interpretation) Regulations 2008.¹⁸⁷ This enabled Westpac and VISA to create a product involving a low-cost remittance card that allowed the recipient to withdraw money deposited by the sender who held the card account, through ATM and EFTPOS networks.¹⁸⁸ Government and regulator involvement in designing innovative financial products may enhance financial inclusion and address the consequences of blanket de-risking policies.

Another way to lower the price of remittances may be for the government to regulate the pricing of remittances — adopting an approach similar to that taken in regulating uncompetitive markets. For example, the government may set a maximum price.¹⁸⁹ It may also set remittance prices to a low fixed amount by regulation, as the cost of providing remittance services does not depend on the amount of the transfer.¹⁹⁰ While price fixing can result in distortions to the market and inefficiency in some cases, it can also result in improvements if there are imperfections in the market or if there is a market failure.

To address the proliferation of informal channels, the United Kingdom government responded to the closure of Somalian money remitters by establishing the Action Group on Cross-Border Remittances, which is overseeing the design of a *safer corridor*¹⁹¹ pilot for United Kingdom–Somalia remittances.¹⁹² This may be adopted in New Zealand for developing, low-risk Asian and Pacific nations.

2 Keep Money Remitters Open

If the government decides to keep money remitters open, it must address the cause of blanket de-risking policies — that is, the high risk posed by money remitters and the resulting unwillingness of banks to retain them as customers.

Intensive regulation and supervision may reduce the risk represented by money remitters. In Australia, money remitters are required to register with AUSTRAC¹⁹³ and reapply for registration every three years.¹⁹⁴

187 Don Abel and Kim Hailwood “The New Zealand-Pacific Remittance Corridor: Lowering Remittance Costs” in Ibrahim Sirkeci, Jeffrey H Cohen and Dilip Ratha (eds) *Migration and Remittances during the Global Financial Crisis and Beyond* (World Bank Group, Washington DC, 2012) 319 at 321.

188 Ooi and Buckley, above n 123, at 254.

189 Dilip Ratha “Remittances: Funds for the Folks Back Home” (28 March 2012) International Monetary Fund <www.imf.org>.

190 Ratha, above n 189.

191 A safe corridor is where a private firm provides remittance services but the transfers are audited at both ends of collection and distribution. See Action Group on Cross Border Remittances *Revised Terms of Reference for the Action Group on Cross Border Remittances* (United Kingdom Government, January 2015).

192 Edwina Thompson and others *Safer Corridors Rapid Assessment: Case Study - Somalia and UK Banking* (Beechwood International, 2013) at 9.

193 Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (Cth), s 74.

194 Sections 75F and 75J.

Registration involves providing information relating to suitability and allowing AUSTRAC to obtain information from third parties to determine suitability. The AUSTRAC CEO is empowered to refuse, suspend, cancel or impose conditions on registration and sanction unregistered money remitters with infringement notices.¹⁹⁵ A recent review of the Australian equivalent of the AML/CFT Act found that stakeholders preferred more intensive regulation, and raised ideas such as:¹⁹⁶

- tiered licensing, with categories of licenses based on the nature and scale of a remitter's business activities and the introduction of caps in the amounts that can be transferred under each category of license
- “fit and proper person” tests to examine the probity and suitability of all key personnel, such as directors, managers, beneficial owners and any other persons who direct or control the business, and
- a technical capacity or competency requirement, where an applicant must demonstrate they understand and can meet the regulatory and compliance obligations to operate a remittance business ...

However, stricter requirements and intensive regulation could increase entry requirements, compliance costs and regulatory expenses. These can discourage competition without necessarily delivering the desired outcomes — money remitters would continue to pose a high risk from their transfers to countries with weak AML/CFT controls. By its design, the AML/CFT regime tends to disproportionately affect “small-scale, localized and personalized” money remitters through high compliance costs.¹⁹⁷ Smaller money remitters would suffer the most if it becomes more complex and costly for them to operate, even if banks become willing to maintain their banking relationships.

The Australian government warned that proposals for new regulation should consider the risk of high-risk customers and money remitters moving to informal, unregulated channels to avoid the burden of supervision.¹⁹⁸ It also noted that evidence from after the 2011 amendments, which introduced registration requirements for money remitters, suggested the remittance sector had grown instead of moving underground.¹⁹⁹ Enhancing regulation could reduce the risks associated with money

195 Sections 75E–75H.

196 Attorney-General's Department, Australia *Report on the Statutory Review of the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 and Associated Rules and Regulations* (April 2016) at 102.

197 Cooper and Walker, above n 5, at 1130.

198 Attorney-General's Department, Australia, above n 196, at 103.

199 At 103.

remitters, but caution should be exercised regarding compliance costs, which may drive closures or movement to informal channels.²⁰⁰

The risk posed by money remitters might also be lowered by placing a low transfer limit on remittance accounts. This would deter criminals, while allowing legitimate remittances. Rebecca Stanley and Ross Buckley argue that remittances amounting to less than USD 750 per day should only require the names of sender and recipient, and the transaction's unique reference number, with the providers not being required to verify this information unless the transaction appears suspicious.²⁰¹ Allowing limits to be exceeded to provide financial aid would ensure flexibility in times of emergency, such as during natural disasters.²⁰² While this limit may be effective for deterring money-laundering activities involving large amounts of money, it is unclear whether it will have the same effect for terrorist financing where recipients aggregate smaller sums of money sent by multiple people, from seemingly legitimate sources. Nonetheless, limits may slow down the flow of terrorist financing without preventing small, innocent transfers.

3 Immediate Steps

The government's immediate response to *E-Trans* should be to review the AML/CFT Act and to set up a safe harbour,²⁰³ regardless of the outcome chosen. A review of the Act would be useful for developing policies to respond to the causes or consequences of blanket de-risking policies, as it would allow consultation with stakeholders. For example, consultation of the statutory review in Australia found that law enforcement and many money remitters supported stronger regulation of the sector, with a stricter licensing regime, greater monitoring powers and greater penalties for unregistered remitters.²⁰⁴ Setting up a safe harbour during the review of the AML/CFT Act may be useful in the short-term while the government sought a longer-term solution.²⁰⁵ This would mean that money remitters could keep their accounts open, notwithstanding the authority of *E-Trans*.

VII CONCLUSION

Blanket de-risking policies against money remitters have serious consequences for society and counterterrorism. The government should intervene via legislation in light of the decision in *E-Trans*. Termination of money remitters' bank accounts could lead to their closures, which would

200 At 103.

201 Stanley and Buckley, above n 89, at 102.

202 At 26.

203 "Safe harbour" policies refer to conferring amnesty from criminal and civil legal actions on a specified set of activities. Durner and Shetret, above n 34, at 30.

204 Attorney-General's Department, Australia, above n 196, at 99.

205 Durner and Shetret, above n 34, at 30.

have negative economic and social impact on migrant communities and recipient countries. Loss of inexpensive and accessible remittances could also lead to a proliferation of informal remittance channels that are unsupervised and pose a greater risk of financing terrorism. The form of legislative intervention depends on the government's desired outcome for money remitters. If the government wishes to keep money remitters open, it must address the causes of blanket de-risking policies. If it wishes to allow them to close, then the consequences of blanket de-risking policies must be addressed. Regardless of the outcome chosen, the government should review the AML/CFT Act and adopt a *safe harbour* measure to ensure innocent transfers are not impeded in the meantime. The AML/CFT regime was designed to starve terrorism of financing. As the fight against terrorism continues around the world, the unintended consequences of the regime must be addressed — especially if it leads to the impoverishment of developing countries and propagation of terrorist financing.