



THE SENATE

LEGAL AND CONSTITUTIONAL AFFAIRS REFERENCES COMMITTEE

## *Discussion paper*

### Inquiry into the adequacy and efficacy of Australia's anti-money laundering and counter-terrorism financing (AML/CTF) regime

The purpose of this discussion paper is to present brief summaries and questions to guide you in preparing your submission. This paper is not intended to be prescriptive, but it should be read in conjunction with the [terms of reference](#). Your submission may go beyond the questions raised in this paper, so long as it remains directly relevant to the terms of reference.

#### **Background**

The [Anti-Money Laundering and Counter-Terrorism Financing Act 2006](#) (AML/CTF Act) commenced operation in December 2006 and established a regime designed to make the Australian financial system hostile to money laundering and terrorism financing threats. The AML/CTF Act is supplemented by the [Anti-Money Laundering and Counter-Terrorism Financing Rules Instrument 2007 \(No. 1\)](#) (AML/CTF Rules).

Several reforms, including legislative changes, have occurred subsequent to enactment of the AML/CTF Act. Much of this reform has been underpinned by/developed in the context of:

- reviews undertaken by the Financial Action Task Force to assess Australia's compliance with FATF Recommendations; and
- recommendations from the *Report on the Statutory Review of the Anti-Money Laundering and Counter-Terrorism Financing Act 2006*.

#### **Financial Action Task Force: Mutual Evaluation Reports and 3rd Enhanced Follow-Up Report**

The Financial Action Task Force (FATF):

is the global money laundering and terrorist financing watchdog. The inter-governmental body sets international standards that aim to prevent these illegal activities and the harm they cause to society. As a policy-making body, the FATF works to generate the necessary political will to bring about national legislative and regulatory reforms in these areas.<sup>1</sup>

The [FATF Recommendations](#) (which 'set out a comprehensive and consistent framework of measures which countries should implement in order to combat money laundering and terrorist financing') include standards for the regulation of Designated Non-Financial

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<sup>1</sup> Financial Action Task Force (FATF), *Who we are*, <https://www.fatf-gafi.org/about/> (accessed 30 July 2021).

Businesses and Professions (DNFBPs) such as real estate agents and jewellers. In summary, these are:

- Customer Due Diligence (CDD) and record-keeping requirements;
- internal control programmes against money laundering and terrorist financing;
- obligations on foreign branches and majority-owned subsidiaries;
- enhanced due diligence measures applicable to relationships and transactions with natural and legal persons and financial institutions from higher-risk countries;
- reporting of suspicious transactions; and
- tipping-off and confidentiality protections.

### **Designated Non-Financial Businesses and Professions (DNFBPs)**

Certain businesses and professions have been identified as being of greater risk of money laundering and terrorism financing. These businesses and professions, described as Designated Non-Financial Business and Professions (DNFBPs), include: casinos, real estate agents, dealers in precious metals and stones, lawyers, notaries, other independent legal professionals and accountants, and trust and company service providers.<sup>2</sup>

In April 2015, the FATF published the [\*Anti-money laundering and counter-terrorist financing measures – Australia: Mutual Evaluation Report\*](#) (2015 MER). The 2015 MER analysed Australia's compliance with the FATF Recommendations and the effectiveness of Australia's AML/CTF regime. The 2015 MER made several findings and identified a number of 'prioritised recommended actions for Australia'.

In November 2018, FATF published its [\*3<sup>rd</sup> Enhanced Follow-Up Report & Technical Compliance Re-Rating\*](#) (3<sup>rd</sup> Enhanced Follow Up Report). The 3<sup>rd</sup> Enhanced Follow Up Report assessed:

- Australia's progress addressing technical compliance deficiencies identified in the 2015 MER; and
- Australia's progress implementing new requirements related to FATF Recommendations that changed since the 2015 MER.

The 3<sup>rd</sup> Enhanced Follow-Up Report concluded that some progress had been made in addressing technical compliance deficiencies identified in the 2015 MER. Australia was re-rated on seven recommendations and remained non-compliant (NC) or partially compliant (PC) on 14 recommendations. The 14 recommendations where Australia remained NC or PC were:

- Assessing risks & applying a risk-based approach (Recommendation 1);
- Customer due diligence (Recommendation 10);
- Correspondent banking (Recommendation 13);
- Wire transfers (Recommendation 16);

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<sup>2</sup> Attorney-General's Department, *Report on the Statutory Review of the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 and associated rules and regulations*, April 2016, pp. 28-29.

- Reliance on third parties (Recommendation 17);
- Internal controls and foreign branches and subsidiaries (Recommendation 18);
- DNFBPs: customer due diligence (Recommendation 22);
- DNFBPs: Other measures (Recommendation 23);
- Transparency and beneficial ownership of legal persons (Recommendation 24);
- Transparency and beneficial ownership of legal arrangements (Recommendation 25);
- Regulation and supervision of financial institutions (Recommendation 26);
- Powers of supervisors (Recommendation 27);
- Regulation and supervision of DNFBPs (Recommendation 28); and
- Sanctions (Recommendation 35).

The technical compliance ratings from the 3<sup>rd</sup> Enhanced Follow-Up Report are summarised below and are available in full [here](#).

**Table 2. Technical compliance with re-ratings, February 2015<sup>1</sup>**

R 1	R 2	R 3	R 4	R 5	R 6	R 7	R 8	R 9	R 10
PC	LC	C	C	C	C	C	LC	C	PC
R 11	R 12	R 13	R 14	R 15	R 16	R 17	R 18	R 19	R 20
LC	LC	NC	LC	C	PC	PC	PC	LC	C
R 21	R 22	R 23	R 24	R 25	R 26	R 27	R 28	R 29	R 30
C	NC	NC	PC	NC	PC	PC	NC	C	C
R 31	R 32	R 33	R 34	R 35	R 36	R 37	R 38	R 39	R 40
LC	C	LC	LC	PC	C	C	C	C	C

*Note:* There are four possible levels of technical compliance: compliant (C), largely compliant (LC), partially compliant (PC), and non-compliant (NC).

### *Questions for consideration*

- To what extent have legislative changes enacted since the 3<sup>rd</sup> Enhanced Follow-Up Report addressed the compliance issues against FATF Recommendations?
- For those FATF Recommendations where Australia remains non-compliant or partially compliant, what are the barriers to achieving compliance?
- To the extent that Australia was assessed as non-compliant or partially compliant, what should be the priority areas? What needs to happen in the short, medium and long term?
- What are the risks to Australia of continued non-compliance or partial compliance with the FATF Recommendations?

The FATF's [2005 MER](#) found Australia was non-compliant or only partially compliant with recommendations pertinent to DNFBPs. The [2015 MER](#) similarly found Australia was largely non-compliant or only partially compliant with recommendations relevant to DNFBPs. The FATF's [3rd Enhanced Follow-up Report & Technical Compliance Re-Rating](#), Australia was assessed as remaining largely non-compliant with recommendations related to DNFBPs. As such, Australia remained in enhanced follow-up.

Since 2018, Australia has taken action on some FATF Recommendations where it was assessed as partially compliant or non-compliant. Significant action has been taken on customer due diligence, correspondent banking, and tipping off and confidentiality. Analysis by the Parliamentary Library indicates that no legislative corrective action appears to have been taken since the 3<sup>rd</sup> Enhanced Follow-up Report on recommendations related to DNFBPs (specifically Recommendations 22, 23, 25, 28 and 35; see earlier section for brief descriptions of these recommendations).

The phased series of reforms to Australia's AML/CTF regime are commonly referred to as 'tranches'. The *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* is referred to as Tranche 1. Further reforms, released in January 2021, to 'increase the resilience of our financial system against criminal threats, while making it easier for businesses to understand and comply with their obligations' are known as Tranche (or Phase) 1.5. Tranche 2 is generally considered to be the AML/CTF regulatory obligations that would apply to DNFBPs.

### ***Questions for consideration***

- What are the impediments to Australia regulating DNFBPs?
- What are the reputational risks to Australia if DNFBPs continue to fall outside the scope of AML/CTF regulation?
- What reasons or explanations have been advanced for Australia not implementing additional legislative corrective action in relation to DNFBPs?
- What are the potential risks, costs or other unintended consequences of poor design or implementation of additional AML/CTF regulation?
- What are the implications for Australia as a competitive global economy and our ability to attract global investment if DNFBPs are not regulated under the AML/CTF regime?
- What has been the experience of other countries with the regulation of DNFBPs and how is this instructive to Australia?

### **Attorney-General's Department statutory review of the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006***

In April 2016, the Attorney-General's Department published its report on a [statutory review](#) of the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (AGD Review). The AGD Review considered:

- the operation of the AML/CTF scheme;
- the extent to which the policy objectives of the AML/CTF regime were appropriate;
- whether the provisions of the AML/CTF regime were appropriate for the achievement of those objectives; and
- the 2015 FATF Mutual Evaluation Report (MER).

The AGD Review made numerous findings and 84 recommendations. Of particular relevance to DNFBPs, the AGD Review found that:

- smaller businesses tend to struggle to identify, understand, manage and mitigate their AMC/CTF risks, and
- smaller businesses tend to seek more prescriptive AML/CTF rules and greater regulatory guidance.

The AGD Review recommended, amongst other things, that the Attorney-General's Department and AUSTRAC develop options for regulating DNFBPs and conduct a cost-benefit analysis of those regulatory options.

In February 2017, the Attorney-General's Department released a [project plan](#) for implementing the recommendations of the 2016 AGD Review in two phases. Cost-benefit analysis of regulatory options for DNFBPs ('Tranche Two entities') was identified as a Phase 1 non-legislative project, slated for completion by June 2017.

### ***Questions for consideration***

- To what extent do recommendations in the 2016 AGD Review remain relevant to the regulation of DNFBPs in Australia?
- To what extent are recommendations from the 2016 AGD Review and the 2017 project plan yet to be implemented?
- In relation to recommendations that remain outstanding, what are the barriers to their implementation?
- Should the implementation of recommendations about DNFBPs be a priority? If so, why?

### **Australian Transaction Reporting and Analysis Centre**

The Australian Transaction Reporting and Analysis Centre (AUSTRAC) is the Commonwealth agency 'responsible for detecting, deterring and disrupting criminal abuse of the financial system to protect the community from serious and organised crime'.<sup>3</sup>

AUSTRAC collects and analyses financial reports and information to generate financial intelligence. This information about potential criminals and criminal activity contributes to national security and law enforcement investigations.

AUSTRAC has a range of responsibilities under the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* and was the focus of the 2016 AGD Review.

### ***Questions for consideration***

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<sup>3</sup> AUSTRAC, *AUSTRAC overview*, available: <https://www.austrac.gov.au/about-us/austrac-overview> (accessed 6 August 2021).

- Is AUSTRAC’s design, operational approach and effectiveness in enforcing existing legislation appropriate for implementing Tranche 2 legislation, investigation and compliance requirements?
- Is AUSTRAC appropriately resourced for implementing Tranche 2?
- Is AUSTRAC’s fit within Australia’s broader financial regulatory ecosystem optimal for implementing Tranche 2?
- Do the regulatory frameworks that exist in other countries (see the ‘International experience’ section following) provide any alternative approaches that should be considered?

### **Australian Taxation Office**

The Australian Taxation Office (ATO) has certain responsibilities under the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006*, for example under the Know Your Customer obligations.

Much of the opposition to implementation of Tranche 2 legislation has focused on the increased costs and burden of new, complicated and overly-onerous compliance regimes. Alternatives might include a nexus between the taxation obligations placed on DNFBPs and AML/CTF regulation.

### ***Questions for consideration***

- Are there alternative taxation and record keeping arrangements that could be implemented with less rather than more complexity?
- Would ATO monitoring of real time tax positions (cashflows) of companies and large individuals provide better scope for detecting laundering?
- Are there international examples of tax regimes that manage to control money laundering without imposing excessive regulatory burdens?
- To what extent do bitcoin and digital currencies require a different approach?

### **International experience**

Each FATF member country is subject to regular evaluations to analyse their compliance with the FATF Recommendations, including through the MER process. Countries similar to Australia that have recently been subjected to a MER include New Zealand, Singapore, the United Kingdom and Canada.

#### *New Zealand*

A [FATF MER](#) published in April 2021 found New Zealand:

has a robust understanding of its money laundering and terrorist financing (ML/TF) risks. It has established a comprehensive multi-tiered risk assessment process, with its national risk assessment (NRA) undergoing two full cycles. National AML/CFT policies and activities address identified ML/TF risks to a substantial extent. Authorities have taken action to

respond to emerging TF risks in the context of a lower overall risk profile. Domestic co-ordination and co-operation are strengths of New Zealand's AML/CFT system.<sup>4</sup>

DNFBPs are covered by the *Anti-Money Laundering and Countering the Financing of Terrorism Act 2009* (NZ); however, the FATF found that:

There remain some gaps in the AML/CFT Act, which impact New Zealand's overall effectiveness. Reporting entities' understanding and implementation of their AML/CFT obligations is mixed, with a better understanding and implementation in larger and more sophisticated reporting entities.<sup>5</sup>

### *Singapore*

A 2016 [FATF MER](#) found that 'Singapore's AML/CFT coordination is highly sophisticated and inclusive of all relevant competent authorities'. In relation to DNFBPs, FATF stated that those in Singapore have:

a less mature understanding of TF risks, and often failed to distinguish between terrorism and TF risks. Overall, there is a significant difference in the level of understanding of the ML/TF risks between the financial sector and DNFBP sector, therefore limiting DNFBPs' ability to develop a comprehensive risk understanding.<sup>6</sup>

FATF also found that:

Singapore has recently extended AML/CFT supervision to most types of DNFBPs, but there are significant differences in effective supervision of AML/CFT requirements between relevant supervisory bodies. While Singapore has a range of remedial measures that it can impose on FIs, the financial penalty structure across the DNFBP sector is quite diverse and concerns exist about the differences in approach in terms of dissuasiveness and proportionality. Apart from the casino and TSP sectors, sanctions for non-compliance by DNFBPs have not been tested.<sup>7</sup>

### *United Kingdom*

In December 2018, a [FATF MER](#) concluded that:

The UK has a robust understanding of its ML/TF risks which is reflected in its public national risk assessments (NRAs). National AML/CFT policies, strategies and activities seek to address the risks identified in the NRAs. National co-ordination and co-operation on AML/CFT issues at both the policy and operational levels has improved significantly since the last evaluation.

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<sup>4</sup> FATF, *Anti-money laundering and counter-terrorist financing measures: New Zealand Mutual Evaluation Report*, April 2021, <https://www.fatf-gafi.org/media/fatf/documents/reports/mer4/Mutual-Evaluation-Report-New-Zealand-2021.pdf> (accessed 30 July 2021), p. 3.

<sup>5</sup> FATF, *Anti-money laundering and counter-terrorist financing measures: New Zealand Mutual Evaluation Report*, April 2021, p. 4.

<sup>6</sup> FATF, *Anti-money laundering and counter-terrorist financing measures: Singapore Mutual Evaluation Report*, September 2016, p. 4.

<sup>7</sup> FATF, *Anti-money laundering and counter-terrorist financing measures: Singapore Mutual Evaluation Report*, September 2016, p. 4.



The UK proactively investigates, prosecutes and convicts a range of TF activity, in line with its identified risks in this area... Another strong point of the system is that all entities within the FATF definition of financial institutions and all DNFBPs are subject to comprehensive AML/CFT requirements and subject to supervision. Supervisors' outreach activities, and fitness and proprietary controls are generally strong. Each supervisor takes a slightly different approach to risk-based supervision. However, while positive steps have been taken, there are weaknesses in the risk-based approach to supervision even among the statutory supervisors.<sup>8</sup>

### *Canada*

A 2016 [FATF MER](#) concluded that:

The Canadian authorities have a good understanding of most of Canada's money laundering and terrorist financing (ML/TF) risks. The 2015 Assessment of Inherent Risks of Money Laundering and Terrorist Financing in Canada (the NRA) is of good quality. AML/CFT cooperation and coordination are generally good at the policy and operational levels.

All high-risk areas are covered by AML/CFT measures, except legal counsels, legal firms and Quebec notaries. This constitutes a significant loophole in Canada's AML/CFT framework.

...

[Financial institutions (FIs)] and DNFBPs are generally subject to appropriate risk-sensitive AML/CFT supervision, but supervision of the real estate and dealers in precious metals and stones (DPMS) sectors is not entirely commensurate to the risks in those sectors. A range of supervisory tools are used effectively especially in the financial sector. There is some duplication of effort between FINTRAC and the Office of the Superintendent of Financial Institutions (OSFI) in the supervisory coverage of federally regulated financial institutions (FRFIs) and a need to coordinate resources and expertise more effectively.

Legal persons and arrangements are at a high risk of misuse, and that risk is not mitigated.<sup>9</sup>

### ***Questions for consideration***

- How does the Australian experience compare internationally?
- Are there unique challenges affecting Australia's ability to implement recommendations from FATF?
- What could Australia learn from international counterparts such as New Zealand, Singapore, the United Kingdom and Canada?
- How does the lack of regulation of DNFBPs in Australia impact its relationships and collaboration with international counterparts, with regard to serious and organised and financial crime?

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<sup>8</sup> FATF, *Anti-money laundering and counter-terrorist financing measures: United Kingdom Mutual Evaluation Report*, December 2018, pp. 3-4.

<sup>9</sup> FATF, *Anti-money laundering and counter-terrorist financing measures: Canada Mutual Evaluation Report*, September 2016, pp. 3-4.



## **Current and emerging challenges in AML/CTF**

During 2021, FATF has produced several publications to highlight emerging challenges in the AML/CTF space, including the [Opportunities and Challenges of New Technologies for AML/CTF](#).<sup>10</sup> In June 2021, FATF published [Outcomes from the June 2021 Plenary](#) which outline FATF's strategic initiatives in several areas, including:

- exploring the opportunities and challenges of digital transformation of AML/CTF;
- virtual assets;
- money laundering from environmental crime;
- ethnically or racially motivated terrorism financing;
- operational challenges with asset recovery;
- guidance on proliferation financing risk assessment and mitigation;
- strengthening measures to prevent the proliferation of weapons of mass destruction; and
- strengthening the FATF standards on beneficial ownership.

### ***Questions for consideration***

- How do the priority areas identified by FATF in 2021 inform Australia's response to emerging challenges in AML/CTF?
- How do the emerging challenges identified by FATF apply in the Australian context?
- Do Australia's weaknesses or lack of compliance with FATF recommendations make us more vulnerable to money laundering activities than comparable economies?
- What learnings are there for Australia from experiences in other nations' implementation of AML/CTF regulation to DNFBPs?
- Are there case studies of direct experiences, especially from overseas countries, which will inform understanding of the key issues?

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<sup>10</sup> A full list of FATF publications is available at the following link: [https://www.fatf-gafi.org/publications/?hf=10&b=0&s=desc\(fatf\\_releasedate\)](https://www.fatf-gafi.org/publications/?hf=10&b=0&s=desc(fatf_releasedate))