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Scope of submission

The Attorney-General's Department (AGD) thanks the House of Representatives Standing Committee on Tax and Revenue for the opportunity to make a submission to its *Inquiry into taxpayer engagement with the tax system*.

Our submission, which includes input from the department's portfolio agencies, the Australian Transaction Reports and Analysis Centre (AUSTRAC), the Australian Criminal Intelligence Commission (ACIC) and the Australian Federal Police (AFP) focuses on the cash economy aspects of the Committee's terms of reference. In particular, we discuss:

- trends in relation to the use of cash in the Australian economy
- the risks associated with the misuse of cash for criminal activity, and
- ongoing regulatory and operational efforts to prevent the criminal misuse of Australia's cash economy.

We note that while the Committee chair, Mr Kevin Hogan MP, requested input from the Attorney-General's portfolio on the cyber safety aspects of Australia's tax system as part of this submission, the Australian Taxation Office (ATO) and the Australian Signals Directorate are the relevant agencies to contact regarding these matters.

Introduction

Cash is the preferred method of payment for goods and services for billions of people around the world. Many of the poorest and least developed countries have economies that are predominantly cash-based. However, cash also continues to be a common method of transferring value in some of the world's largest and most developed economies.¹ Transaction data collected by AUSTRAC over the past five years suggests that Australia is no exception, with cash continuing to be a popular and widely used method of payment.

While a significant amount of the cash currently in circulation is used for legitimate purposes, the criminal economy remains predominantly cash-based.² Criminal groups continue to require effective channels to 'place' cash into the financial system, and for this reason, they have proven historically to be highly adaptable

¹ Financial Action Task Force (FATF), 'Money Laundering through the Physical Transportation of Cash', October 2015, available at <http://www.fatf-gafi.org/media/fatf/documents/reports/money-laundering-through-transportation-cash.pdf>, page. 27.

² FATF, Money Laundering through the Physical Transportation of Cash, page. 27.

in order to exploit changing circumstances. Criminal misuse of the cash economy affects government revenue and has broader implications for the integrity of Australia's financial system.

However, tougher domestic and international regulations on the use of cash and continued close scrutiny from law enforcement agencies will ensure that the Australian Government remains well-equipped to combat this ongoing threat.

Australia's cash economy

A key element of Australia's anti-money laundering and counter-terrorism financing (AML/CTF) regime is the requirement for regulated businesses to perform customer due diligence, retain records, and report specified transactions to AUSTRAC. As Australia's financial intelligence unit (FIU) and AML/CTF regulator, AUSTRAC's purpose is to protect the integrity of Australia's financial system and contribute to the administration of justice through its expertise in countering money laundering and the financing of terrorism.

In its FIU role, AUSTRAC collects analyses and transforms financial information from over 14,000 Australian businesses into 'actionable intelligence' for the ATO, other Australian law enforcement, intelligence, regulatory and border agencies and for international counterpart FIUs. This intelligence is used to investigate and prosecute serious criminal activity, including money laundering, terrorism financing, organised crime and tax evasion.

A key obligation for these businesses is the collection and reporting to AUSTRAC of financial transaction and suspicious matter reports (SMRs). These reports allow AUSTRAC to closely monitor the movement and use of cash in the Australian economy. Each year AUSTRAC disseminates thousands of pieces of actionable intelligence to its partners, including SMRs and detailed analysis reports, for use in their investigations and operations. This includes methodologies briefs so they can better tailor SMR quality against high-priority threats.

The actionable financial intelligence disseminated by AUSTRAC contributes to investigations and related seizures of criminal proceeds and revenue by law enforcement, national security, revenue authorities, border protection and other agencies in Australia and overseas. Over the last 10 years the use of AUSTRAC information and intelligence contributed to additional tax assessments and debt collections of nearly \$2.8 billion.

To assist the Committee in its understanding of the prevalence of the use of cash in the Australian economy, our submission considers the trends evident in reports submitted to AUSTRAC in the period from 2011-2016, including:

- *threshold transaction reports (TTRs)*: reporting entities must report transactions involving the transfer of physical currency or e-currency of \$10,000 or more
- *cross-border movement reports (CBMs)*: travellers must report cross-border movement of physical currency of AUD10,000 or more (or foreign currency equivalent) and, on request, cross-border movement of bearer negotiable instruments of any amount
- *international funds transfer instructions (IFTIs)*: reporting entities must record the sending/receipt of funds into/out of Australia, irrespective of the value, and
- *SMRs* by reporting entities.

Trends in the use of cash

AUSTRAC data indicates a steady decrease in the use of cash throughout the period from 2011-2016. During this time, TTRs declined in both volume and value from 5.23 million reports (total value \$228.8 billion) in 2011 to 4.59 million reports (total value \$160.71 billion) in 2016 (a 12.2% decrease in volume and 29.76% decrease by value).³

Despite this overall trend, the value of reporting indicates the continuing prevalence and use of cash in Australia.

The reduction in the number and value of TTRs since 2011 has been driven largely by the decreasing number of reports submitted by the cash-carrying industry which, together with the banking sector, accounts for the bulk of threshold reports. While the volume and value of TTRs submitted by banks have also decreased over the period, this is driven by the decrease in TTRs related to incoming transactions (i.e. account deposits) between 2011 and 2016. Banks have submitted an increased number of TTRs for outgoing transactions (i.e. account withdrawals) during the same period.

This reporting pattern may reflect similar factors to those identified as possibly contributing to the increase in the number and value of banknotes in circulation from 2011-2016. While the use of cash for transactions has been decreasing, there is likely a higher use of cash as a store of value in the domestic economy, an increase

³ Such data is consistent with data published by the Reserve Bank of Australia indicating a drop from \$150.7 billion withdrawn from ATMs in 2011-2012 to \$138.7 billion withdrawn from ATMs in 2015-2016 (a decrease of 7.9%). The reduction in ATM withdrawals suggests that the reduction in the use of cash is not confined to transactions over \$10,000.

in foreign demand and the continuing use of cash for unlawful purposes.⁴ AUSTRAC data also reveals a contemporaneous increase in the number and value of CBMs over the 2011-2016 period from \$2.44 billion in cash or bearer negotiable instruments reported entering or leaving Australia in 2011 to \$9.28 billion in 2016.

Trends in non-cash transactions

AUSTRAC data on the use of electronic payments is derived primarily from IFTIs.⁵ AUSTRAC's IFTI reporting data is consistent with a broader shift towards electronic payments. IFTI reporting (both incoming and outgoing) increased from 33.66 million reports submitted in 2011 to 102.94 million reports in 2016, a threefold increase. At the same time, the value of IFTI reports has risen from \$3.5 trillion in 2011 to \$4.7 trillion in 2016, an increase of approximately one third. The divergence between the increases in volume and value is explained in part by the increase in on-line micropayments during that period.

Trends in reporting of tax evasion related SMRs

The number of SMRs submitted to AUSTRAC relating to possible tax evasion offences has remained largely consistent during the 2011-2016 period at between 2,400 to 3,500 reports annually. The total value of the transactions to which the SMRs relate has increased from \$540 million to \$1.3 billion.⁶

Criminal exploitation of Australia's cash economy

Money laundering

Money laundering offers an attractive means for criminals seeking to hide the illegitimate source of cash generated from illegal activities such as tax evasion, drug trafficking, fraud and corruption. By cleaning and intermingling the proceeds of crime into the legitimate financial system, money laundering enables additional serious criminal activity and allows criminals to hide and accumulate wealth, avoid prosecution and evade taxes.

⁴ Davies, C, Doyle M-A, Chay, F and Nightingale, S, 'The Future of Cash', *The Bulletin*, December Quarter 2016, Reserve Bank of Australia. The authors note, however, that due to the anonymous nature of cash it was not possible to accurately measure these various sources of demand.

⁵ Domestic electronic payments will only be reported to AUSTRAC where they are captured by one of the other reporting obligations, e.g. if cash exceeding the TTR threshold is used at any point in the transaction or the payment is reported as an SMR.

⁶ SMRs are not, in and of themselves, evidence of the commission of tax evasion offences, but indicate suspicions by regulated businesses.

The ACIC has identified that cash businesses present a variety of opportunities to launder money, with a number of case studies being identified whereby:

- illicit funds are mingled with legitimate business earnings
- illicit funds are used to purchase stock, equipment and premises which in turn can increase the re-sale value of that business, and
- false sales records are created to inflate business turnover which allows the injection of illicit funds.

Organised criminals also exploit the Australian taxation system by using increasingly complex and sophisticated organisational structures – making these entities less recognisable and harder to detect. ACIC intelligence suggests that organised criminals are commonly using one of Australia’s most common forms of business structure, the sole trader (which makes up the highest proportion of registered businesses in the country), to facilitate illicit activity. This type of structure is predominantly used to operate businesses in cash-intensive industries, and these industries are attractive to organised crime because of the relatively untraceable nature of cash transactions and the opportunities to commingle illicit and legitimate funds. Organised crime groups can create multiple sole trader entities in order to facilitate tax evasion or money laundering activities.

ACIC intelligence also suggests that the construction industry provides considerable scope to launder money, for example, via paying tradespeople in unrecorded cash for part of their work or paying for part of the cost of materials in unrecorded cash. This in turn causes the cost of construction and renovations to be understated so that an artificially large profit will be created.

Identity crime

Organised criminals can also exploit business and company registration processes through the use of identity crime, fictitious names or the placement of ‘straw’ or nominee proprietors or company office holders. Law enforcement investigations have typically shown organised crime to be involved in operating cash businesses.

Fraudulent identities have also been used to commit welfare, tax and other fraud against government agencies, gain unauthorised access to sensitive information or facilities, conceal other criminal activities such as drug trafficking, and even to facilitate the commission of terrorist acts. The costs associated with detected identity crime incidents can be substantial. For example, based on data provided as part of *the Identity Crime and Misuse in Australia* report in 2014-15, the ATO saved \$8.7 million in protected revenue as a result of identity fraud protective measures that disrupted attempts to claim returns using stolen identities. This is based on 146,279 incidents of potentially compromised Tax File Numbers identified by the ATO. Further to

this, in 2015-16 IDCARE, an independent support service for victims of identity crime, provided 1,001 hours of Identity Security Counselling Support to 1,432 ATO clients.

Responses to emerging trends

Statutory review of Australia's AML/CTF regime

The report on the statutory review of Australia's AML/CTF regime was tabled in Parliament by the Minister for Justice in April 2016. The review concludes that Australia's AML/CTF regime remains robust and relevant but identifies opportunities to make further enhancements. The recommendations arising from this review are designed to strengthen measures to protect the Australian community and financial system, and better position law enforcement agencies to respond to new and emerging threats. Key measures relating to the cash economy include proposals relating to the regulation of high-value dealers (HVDs) and enhanced information sharing.

High-value dealers

The report of the review highlights the money laundering risks posed by the buying and selling of high-value goods (HVGs)⁷ using large sums of cash.⁸ Buying and selling HVGs is recognised internationally as a major avenue for money laundering activity. HVGs are vulnerable to misuse for money laundering purposes because they can be bought anonymously using cash to either use, or sell, with the money gained being reinvested elsewhere, and the origin of the illicit cash obscured.

Consistent with the global AML/CTF standards set by the Financial Action Task Force,⁹ more and more countries are regulating HVDs (businesses involved in the buying and selling of HVGs) for AML/CTF purposes. The regulation of HVDs delivers a number of benefits. In particular, it can discourage the HVD sector from accepting large cash payments to avoid AML/CTF regulation. Countries which regulate HVDs also become more hostile to money laundering threats, enhancing the integrity and credibility of their financial institutions and financial system and increasing the attractiveness of their jurisdiction as a place to conduct business.

The report of the review recommended that a cost-benefit analysis of regulating a number of currently unregulated sectors (including HVDs) be conducted to accurately determine the regulatory impact and the

⁷ HVGs are commonly considered to include jewellery, antiques and collectibles, fine art, yachts and luxury motor vehicles.

⁸ *Report on the Statutory Review of the Anti-Money Laundering and Counter Terrorism Financing Act 2006 and Associated Rules and Regulations*, available at:

<https://www.ag.gov.au/Consultations/Pages/StatReviewAntiMoneyLaunderingCounterTerrorismFinActCth2006.aspx>, see pages 38-39.

⁹ FATF, *The FATF Recommendations, international standards on combating money laundering and the financing of terrorism and proliferation*, available at the following link: [http://www.fatf-gafi.org/publications/fatfrecommendations/?hf=10&b=0&s=desc\(fatf_releasedate\)](http://www.fatf-gafi.org/publications/fatfrecommendations/?hf=10&b=0&s=desc(fatf_releasedate)).

expected benefits. In view of this, AGD is currently consulting with industry to inform the cost-benefit analysis. The cost-benefit analysis is being undertaken by an independent consultant, which will report to the Minister for Justice to inform the decision by the Australian Government on the proposed regulation of HVDs under the AML/CTF regime.

Information sharing

The nature and sophistication of financial crime is continually evolving, and AUSTRAC's capacity to effectively share timely and relevant information with other agencies and the private sector will only increase in importance. As such, the statutory review recommended a comprehensive overhaul of the secrecy and access provisions under Part 11 of the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006*, with a view towards establishing a more flexible and effective framework for sharing AUSTRAC information, including with the private sector.¹⁰

This recommendation would enhance AUSTRAC's ability to disseminate intelligence information to its regulated population. This will assist them to strengthen and enhance their awareness of money laundering and terrorism financing risks, identify new and emerging threats and implement more effective processes to detect and disrupt associated financial crimes. The report on the review of the AML/CTF regime also includes a specific recommendation recognising the potential public benefits of making aggregated AUSTRAC data more available. AUSTRAC is committed to implementing innovative and collaborative approaches that leverage public and private sector partnerships with the aim of improving the prevention of financial crime, and where prevention is not possible, the better detection and disruption of illicit activities.

Identity security

Identity verification is an important part of efforts to prevent identity crime and promote trust and confidence in identities. AGD has been working closely with the ATO on a number of initiatives that fall under the National Identity Security Strategy; these include implementation of the National Identity Proofing Guidelines (NIPGs) and using the Document Verification Service (DVS). The NIPGs provide a set of transparent recommended processes and requirements for identity verification for organisations which issue identity documents. These have been adopted by the ATO.

The ATO uses the DVS as part of their online identity proofing process for new clients. The DVS is a secure, online system that provides for automated checks of the accuracy and validity of information on the key government documents commonly presented as evidence of identity. The DVS enables organisations such as

¹⁰ *Statutory Review Report*, see Chapter 14.

the ATO to check the information on identity credentials against the records of the issuing agency quickly and accurately, providing a trusted online channel for taxpayers to interact with the ATO.

AGD has also been working with the ATO to explore the scope to use new technologies to further strengthen identity proofing process, such as facial biometrics through the Face Verification Service (FVS). The FVS, launched in November 2016, is a one-to-one image based verification service that can match a person's photo against an image on one of their government records to verify their identity. The FVS complements the DVS by helping to prevent identity take-over, where an individual's biographic details are stolen and used with an image of another person. The initial FVS provides select Australian Government agencies with access to citizenship and immigration images held by the Department of Immigration and Border Protection. Other types of images such as passport photos will be added over time, with access expanded to other government agencies.

Operational initiatives

Targeting Criminal Wealth No. 2 Special Investigation

The Targeting Criminal Wealth (TCW) No. 2 Special Investigation into financially motivated crime is designed to disrupt and deter criminal groups by collecting evidence and intelligence about criminal activity.

Almost all organised crime is motivated by profit. Providing intelligence to identify and stop criminal money flows is one of the most effective ways to disrupt the activities of serious and organised crime networks and reduce the harm they cause. This broad special investigation into financially motivated crime brings together the ACIC's work in investigating money laundering, serious and organised superannuation and investment fraud, sophisticated tax evasion and confiscating criminal wealth.

The work of the Special Investigation incorporates the work of several multi-agency national task forces, including the Criminal Assets Confiscation Taskforce and the Serious Financial Crime Taskforce.

Prior to its conclusion in December 2016, the Eligo 2 National Task Force was also incorporated into the TCW No. 2 Special Investigation.

Eligo 2 National Task Force

The Eligo National Task Force (Eligo) was originally authorised in December 2012 as a nationally coordinated preventative taskforce to tackle the high-risk alternative remittance sector and operators of other informal value transfer systems impacting on Australia.

On 9 September 2014, the Eligo 2 National Task Force (Eligo 2) was established to disrupt high-priority international and domestic money laundering operators. The objective of this task force was to take

coordinated collective action against money launderers to reduce their adverse impact on Australia and its national economic wellbeing. Eligo 2 concluded on 31 December 2016.

The Eligo and Eligo 2 Task Forces have provided valuable intelligence insights into ever-changing money laundering methodologies, which in turn inform the responses of the ACIC and its partners.

Together, the Eligo and Eligo 2 Task Forces have delivered the:

- seizure of illicit drugs and precursors with a combined street value of more than \$1.7 billion
- seizure of more than \$85 million in cash
- restraint of more than \$65 million worth of assets
- disruption of 87 serious and organised crime groups and/or networks
- identification of more than 544 targets previously unknown to law enforcement
- identification of eight clandestine drug laboratories, and
- the arrest of 494 people on 1,131 charges.

The Eligo results affirm the value of applying an investigative strategy of following the money as an effective way of unearthing organised criminal activity, including money laundering methodologies.

Criminal Assets Confiscation Taskforce

The Criminal Assets Confiscation Taskforce (CACT) is a multi-agency taskforce led by the AFP which also includes the ATO and ACIC. The CACT is a Commonwealth initiative dedicated to disrupting, deterring and reducing serious and organised crime by taking away the benefits derived from crime and preventing the reinvestment of illicit profits in criminal activity.

The CACT was established in March 2011 with all agencies sharing a common overarching goal; to draw upon different skills, roles and perspectives to enhance the CACT's collective ability to target the criminal economy.

The CACT identifies the most effective and appropriate enforcement strategy for each individual case. This may be through proceeds of crime action; application of taxation remedies or other Commonwealth debt recovery, and/or recovery through relevant state, territory or foreign law enforcement agencies.

Serious Financial Crime Taskforce

The Serious Financial Crime Taskforce (SFCT) is a multi-agency group that forms part of the AFP-led Fraud and Anti-Corruption Centre. The SFCT has been established to bring together the knowledge, resources and experiences of federal law enforcement and regulatory agencies to identify and address serious and complex financial crimes. The SFCT has also been tasked with coordinating Australia's response to the release of the 'Panama Papers', which revealed the myriad ways that high-net worth individuals and corporations exploit complex corporate structures and secretive offshore tax regimes to conceal wealth.

Agencies forming the SFCT include the:

- Australian Federal Police
- Australian Taxation Office
- Australian Criminal Intelligence Commission
- Attorney-General's Department
- Australian Transaction Reports and Analysis Centre
- Australian Securities and Investments Commission
- Commonwealth Director of Public Prosecutions, and
- Australian Border Force.

The SFCT builds on the success of Project Wickenby, which as at 30 June 2015 had resulted in the conviction and sentencing of 46 individuals and the recovery of over \$985 million in outstanding revenue. This includes \$607 million in cash collections, \$372 million from increased voluntary compliance and \$5 million in assets recovered under Commonwealth proceeds of crime provisions.

While Project Wickenby focused on tackling offshore tax evasion and crime, the SFCT has a broader remit to target serious financial crimes of the highest priority. These priorities include international tax evasion and criminality related to fraudulent phoenix activity, trusts and superannuation.

The SFCT focuses on operational activities, the collection and sharing of intelligence, the identification of potential reform measures with the aim to remove wealth from criminal activity, prosecuting facilitators and promoters of serious financial crime and the deployment of deterrent and preventative enforcement strategies. As part of its contribution to the SFCTF, AUSTRAC disseminates monthly reports targeting the cash economy.

Conclusion

The continued criminal misuse of cash in the Australian economy presents a number of ongoing challenges. Cash and cash-intensive businesses provide criminal actors with unique opportunities to launder the proceeds of crime, engage in identity fraud and evade tax.

While the regulatory environment remains dynamic and challenging, Australian Government agencies continue to respond collaboratively and flexibly to this ever-changing threat.