14 October 2024

Committee Secretary
Senate Legal and Constitutional Affairs Committee
PO Box 6100
Parliament House
Canberra ACT 2600

By email: legcon.sen@aph.gov.au

Dear Committee

Reference of the Anti-Money Laundering and Counter-Terrorism Financing Amendment Bill 2024 (Bill) to Legal and Constitutional Affairs Legislation Committee

The Financial Services Council (FSC) is a peak body which sets mandatory Standards and develops policy for more than 100 member companies in one of Australia's largest industry sectors, financial services. Our Full Members represent Australia's retail and wholesale funds management businesses, superannuation funds and financial advice licensees. Our Supporting Members represent the professional services firms such as ICT, consulting, accounting, legal, recruitment, actuarial and research houses[1].

The FSC appreciates the opportunity to make a submission to the Committee on the Bill and the explanatory memorandum (EM).

Summary

The FSC commends the hard work and effort that has gone into producing the Bill to amend the Anti-Money Laundering and Counter-Terrorism Financing Act (AML/CTF Act) and supports the underlying intent to simplify and modernise Australia's AML/CTF framework.

However, we are concerned that the regulatory burden and impact of the reforms is significant, and most reporting entities will need more time to assess the design and operational impacts of the changes (notably regarding new requirements for AML/CTF programs, approval processes and CDD requirements). Accordingly, in our view a measured approach to enforcement action and publication of Policy Principles should be considered by the Committee.

Given the importance of the amended Anti-Money Laundering and Counter-Terrorism Financing Rules

[1] The financial services industry is responsible for investing more than $3 trillion on behalf of over 15.6 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange and is one of the largest pool of managed funds in the world.

The FSC's mission is to assist our members achieve the following outcomes for Australians:
- to increase their financial security and wellbeing;
- to protect their livelihoods;
- to provide them with a comfortable retirement;
- to champion integrity, ethics and social responsibility in financial services; and
- to advocate for financial literacy and inclusion

(AML/CTF Rules) to enable regulated entities to properly assess the scope of the Bill and determine what changes they will need to make to comply with their revised obligations, it is also important that the draft amended AML/CTF Rules are released for consultation and engagement with industry as soon as practicable.

In addition, the FSC submits that there are a number of areas where the explanatory memorandum could also be enhanced to provide greater clarity, which we expand upon in the following paragraphs.

Finally, given the significant changes and Impact of the Bill, a statutory review of the revised AML/CTF Act and related Rules should be undertaken within 7 years.

General comments

Implement a Policy Principles period

Although the object of the reforms is to simplify the framework, the FSC submits that the transition will require considerable uplift for existing regulated entities. The planned implementation date of 31 March 2026 for some core reforms (notably changes to CDD) are considered ambitious given their implementation by industry is heavily dependent on the content of the Anti-Money Laundering and Counter-Terrorism Financing Rules (AML/CTF Rules), the content and timing of which remains uncertain. The FSC submits that most reporting entities will need more time to assess the design and operational impacts of the changes on their AML/CTF Programs once the AML/CTF Rules have been finalised and then implement the required changes. Some of the proposed changes are likely to have system impacts for reporting entities (particularly in relation to customer onboarding, due diligence and risk rating).

We note that the original AML/CTF Act was implemented in a staggered manner from 2006 with all provisions fully operational from 12 December 2008. As noted in the *Report on the Statutory Review*[2], in 2006, Policy Principles were issued to give effect to a Government undertaking that the AUSTRAC CEO would only take civil penalty action against a reporting entity, rather than criminal enforcement activity, where that reporting entity has failed to take reasonable steps towards compliance with its obligations under the AML/CTF Act during a 15 month period following commencement of the obligations under the Act. This approach was also taken in 2021-22 with the introduction of reforms to correspondent banking arrangements[3].

The FSC **recommends** that a measured approach to enforcement action and publication of Policy Principles be considered by the Committee.

Release draft AML/CTF Rules and develop guidance as soon as practicable

Given the importance of the AML/CTF Rules to enable regulated entities to assess and determine the regulatory impacts to meet the revised obligations, it is important that the draft AML/CTF Rules are released for consultation and engagement with industry as soon as practicable. We provide further detail on this point below, see "AML/CTF programs and business groups", "New CDD requirements" and "Initial CDD – Delay".

Similarly, the content of AUSTRAC guidance will be pivotal to the implementation of the content of the Bill

[2] Report On The Statutory Review Of The Anti-Money Laundering And Counter-Terrorism Financing Act 2006 And Associated Rules And Regulations (homeaffairs.gov.au)
[3] Anti-Money Laundering and Counter-Terrorism Financing (Correspondent Banking) Policy Principles 2021

and accompanying AML/CTF Rules. It is important that AUSTRAC guidance is developed with input from industry as soon as practicable.

The FSC **recommends** that the draft AML/CTF Rules are released for consultation and engagement with industry as soon as practicable.

Include a statutory review requirement

The Bill is a critical piece of legislation that is intended to simplify and modernise Australia's AML/CTF Regime. Once implemented, it is important that its impact is carefully assessed and reviewed after a suitable period has passed to determine whether it is achieving its intended objectives. When the current legislation was first enacted in 2006, it contained a provision (section 251) for the Minister to initiate a review of the operation of the Act, Regulations and Rules.

The FSC **recommends** that the Committee consider whether a provision be added to enable the appointment of an independent person to conduct a statutory review of the revised AML/CTF Act and related Rules within a period of no more than 7 years after the legislation comes into force.

AML/CTF programs: (i) business groups and (ii) policies, procedures, systems and controls

(i) Business Groups

Much of the content of Schedule 1 is dependent on the AML/CTF Rules. For example, the Bill updates the current definition of a 'reporting entity' in section 5 of the AML/CTF Act to also include the lead entity of a reporting group, and that such a group may be formed when at least one member of a business group provides designated services. The AML/CTF Rules will specify how the lead entity in any reporting group is to be identified. Similarly, the AML/CTF Rules will need to provide much of the detail section 26F (*reporting entities must develop and maintain AML/CTF policies*). Accordingly, it is important that the relevant provisions in these rules are discussed with industry as soon as practicable.

(ii) Policies, Procedures, Systems and Controls

The Bill under proposed Part 1A, Divisions 1 to 3 –introduces an enhanced obligation concerning the requirements for a reporting entity to include as part of its AML/CTF Program:

- A money laundering and terrorism financing risk assessment; and
- AML/CTF policies, procedures, systems, and controls, to be known as AML/CTF policies.

Paragraphs 26F-G of the Bill provide that the reporting entity Is required to develop and maintain AML/CTF policies to achieve among other things the following outcomes:

- to appropriately manage and mitigate the ML/TF risks that the reporting entity may reasonably face in providing its designated services (i.e., ML/TF risk management and mitigation policies).
- to ensure the reporting entity complies with the AML/CTF Act, Rules, and regulations (i.e., ML/TF internal compliance management policies).

The Bill provides that ML/TF risk management and mitigation policies must cover a range of areas outlining *how* the reporting entity will go about meeting its compliance obligations. It is our view that there is a clear

distinction between policy and procedure documents. A policy sets out the overall guideline that a reporting entity must follow to comply with its regulatory obligations. In contrast, procedures set out step-by-step instructions on how to implement the policy. In this context it should be noted that the underlying rationale behind the risk-based approach to AML/CTF obligations by the Financial Action Task Force is that the intention is the reporting entity must determine, on a risk-sensitive basis, *how* it will meet their compliance outcomes.

The FSC **recommends** that a breach of a failure to adhere to procedures should not constitute a breach of the AML/CTF Act and result in penalty provisions.

Proliferation financing

Subsection 26F(11) provides that a reporting entity is not required to develop or maintain specific AML/CTF policies to mitigate and manage proliferation financing risk if it has assessed under subsection 26C and 26D that risk to be low and that it can be appropriately managed by existing policies for ML/TF. The FSC suggests that the EM provide some brief commentary on the types of factors that might point towards low risk (for example, large superannuation funds' risk of proliferation financing might be assessed as low, noting there is an existing robust framework already in place which restricts access to superannuation) which can then be developed in AUSTRAC guidance.

In addition, subsection 26F(12) provides that the reporting entity bears the legal burden of proof to rely on this exception. The EM comments at paragraph 106 that they must assess their risk as low and "*this will be within the reporting entity's knowledge, making the reversal of the burden of proof appropriate*." The FSC notes however that reporting entities will inevitably only have limited knowledge of the wider risks involved and suggests that further detailed justification be provided as to appropriateness of reversing the burden of proof, particularly given the high civil penalty that can be imposed.

The FSC **recommends** that the EM provide further justification as to appropriateness of reversing the burden of proof and should explicitly address relevant principles as set out in the Attorney-General's Department's *Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers.*

The EM indicates that reporting entities consult AUSTRAC's *Proliferation Financing in Australia National Risk Assessment, published in December 2022*, and in this regard the FSC also **recommends** that there be a requirement to update and publish this risk assessment on a fixed recurring basis to ensure that industry has access to up-to-date risk analysis.

Senior managers

The FSC notes that section 26P provides that the ML/TF risk assessment and its AML/CTF policies, and any updates to either, must be approved by a senior manager in the reporting entity, while the governing body must be notified of approved updates to provide effective strategic oversight. The definition of senior manager per section 5 is "an individual who makes, or participates in making, decisions that affect the whole, or a substantial part, of the business of the reporting entity", and the EM states that "*In a large organisation, a Senior Manager may be an employee who does not sit on the board of directors but is responsible for relevant activities of the reporting entity*".

The question arises for large organisations, where they have multiple senior management levels, where would it be appropriate to allocate this function – e.g. would this sit with an individual at the Group

Executive level who reports to the CEO? For large organisations (organisations comprising of thousands of employees), the AML/CTF Compliance Officer may be distinct from other members of Group Executives and therefore not likely to be nominated as the "Senior Manager" for the purpose of approving AML/CTF policies.

The FSC **recommends** that some further brief commentary is provided in the EM on allocating senior managers to approve ML/TF risk assessments and AML/CTF policies, which can then be further developed in AUSTRAC guidance.

New CDD requirements

The FSC notes that the Bill seeks to reframe and clarify the core requirements for initial CDD and ongoing CDD, clarify when enhanced CDD must be applied, and streamline the circumstances when simplified CDD may be applied. Section 28 establishes the principal obligation for undertaking initial CDD. Principle obligations are established for initial CDD, ongoing CDD, enhanced CDD and simplified CDD.

The detail that is to be specified in the AML/CTF Rules is again key to understanding what is required, notably sections 28(6) and 28(7) (Undertaking initial customer due diligence), 29 (Exemptions from initial customer due diligence), 30(2), 30(3), 30(4) (Undertaking ongoing customer due diligence) and 31 (Simplified customer due diligence). Until industry has sight of the proposed Rules, it is difficult to form a meaningful assessment of the changes that will be required. The EM states at paragraph 169 "*…. the amendments simplify the existing AML/CTF regime by clearly stating the outcomes to be achieved by initial CDD, rather than focusing on the procedures. This provides greater flexibility to reporting entities in the steps they take to know their customers*." However, the FSC has concerns that the level of detail that is provided in the AML/CTF Rules will result in added complexity and reduced flexibility for industry.

At paragraph 213 the EM states "i*t is not expected that a reporting entity undertake a bespoke 'risk assessment' for each customer."* The FSC suggests that the Committee consider whether this statement should be included in the Bill itself for clarity and to alleviate any concerns within industry that they will in fact have to make their AML/CTF programs unduly bespoke. The FSC is concerned that the new requirements regarding CDD will in practice result in reporting entities making substantive changes to their AML/CTF programs to address a perceived expectation that reporting entities must move away from existing standardised procedures and controls towards overly bespoke and tailored processes that correspond to different levels of risk posed in a given situation. These changes would take time and resources to implement, introducing increased complexity in the design and operational aspects of CDD Programs (including customer risk rating approaches), and potentially reduce existing efficiencies.

In view of the level of detail that remains to be provided and the current uncertainty as to content and timing of their finalisation, the FSC submits that the Committee consider providing for a longer implementation period for industry for these provisions in the Bill. Given the significant nature of the changes contemplated by the Bill that need to be read with (as yet unseen) AML/CTF Rules and AUSTRAC guidance, it is questionable that industry will be ready to implement these changes by March 2026.

The FSC **recommends** that a longer implementation period is provided to industry for the aforementioned new CDD requirements in the Bill.

CDD - trustees and other relationships

The FSC notes that section 28 of the Bill establishes the principal obligation for undertaking initial CDD. In this

regard, subsection 28(2) sets out the matters that must be established on reasonable grounds, including per the EM at paragraph 208 …." *the identity of any person on whose behalf the customer is receiving the designated service (for example, a trustee receiving a service on behalf of beneficiaries…"*

Given that the EM provides one example which then raises the question as to what else might be contemplated, the FSC submits that further clarity be provided in the EM as to what other types of relationships (apart from trusts) are intended to be covered by this limb.

In addition, the FSC notes that section 28(2) includes determining whether…."any person acting on behalf of the customer is a politically exposed person…". Current requirements are that reporting entities must reasonably determine whether a customer or the customer's beneficial owner are politically exposed persons (PEPs).

Section 28(2) now requires reporting to establish whether anyone acting on behalf of the customer is a PEP. This could be a wide range of people that may be assisting a customer in receiving a designated service, including a person acting under a power of attorney or any other form of agent. These parties may not necessarily be 'beneficial owners' of the customer. This appears therefore to be an expansion of existing requirements, with screening system implications for reporting entities.

In view of this change, the FSC **recommends** that the EM include an additional brief paragraph clarifying these points.

Initial CDD - delay

The FSC notes that section 29 sets out when reporting entities may delay initial CDD, or parts of initial CDD, until after commencing to provide a designated service, in certain circumstances to be specified in the AML/CTF Rules. Subsections 29(1)(a)-(f) clarify that this section applies if:

- the circumstances in the rules apply
- the reporting entity determines on reasonable grounds that commencing to provide the designated service prior to undertaking initial CDD is essential to avoid interrupting the ordinary course of business
- the reporting entity has policies to comply with initial CDD requirements in relation to the customer as soon as reasonably practicable after commencing to provide the designated service, and within any period specified in the AML/CTF Rules
- the difference in ML/TF risk arising from any delay in completing initial CDD is low (as opposed to the customer being identified as low ML/TF risk)
- the reporting entity implements AML/CTF policies to mitigate and manage the associated risks, and
- the reporting entity complies with any requirements specified in the AML/CTF Rules.

The content of the AML/CTF Rules in respect of delayed CDD is again critical to understanding the ambit of these provisions[4]. What constitutes "reasonable grounds" for determining that commencing to provide the designated service prior to undertaking initial CDD is essential to avoid interrupting the ordinary course of business should be developed in guidance following feedback from industry.

[4] The FSC agrees in principle that the AML/CTF Rules should include provision allowing verification of PEP status or whether the person is designated for targeted financial sanctions on 'day 2', where appropriate to the ML/TF risk of the customer and the additional risk from delay is managed and mitigated.

Tipping off offence

We refer to the current tipping off provisions contained in section 123 of the AML/CTF Act and notes that subsection 123 (9) states that the tipping off offence under s123(1) does not apply to the disclosure of information by a reporting entity if:

(a) the disclosure is in compliance with a requirement under a law of the Commonwealth, a State or a Territory; or
(b) the disclosure is to an Australian government body that has responsibility for law enforcement.

Presumably disclosures made in compliance with the proposed Scams Protection Framework (SPF) would fall within the above exemption.

However, the proposed tipping off provisions in the Bill do not contain such an express exemption. The EM does provide examples of where disclosure of information is not intended to constitute tipping off under the reframed offence, including:

- disclosure of information to Australian law enforcement, regulatory or oversight agencies; and
- disclosure of information in compliance with a requirement under a law of the Commonwealth, a State or Territory

The FSC **recommends** that the EM clarify whether proposed regulations (per section 123(5) of the Bill) or guidance from AUSTRAC will expressly address this point. Doing so would give reporting entities some additional level of comfort and clarity.

International value transfer services and reporting obligations

The Bill should clarify the application of these obligations and particularly the content of subsection 63A when read alongside the existing definition of "financial institution" [5] as set out in the AML/CTF Act to remove concerns that certain businesses (which may in a broader sense be considered financial institutions but do not fall within the statutory definition contained in the AML/CTF Act) may be inadvertently caught by the new framework.

Subsection 63A(4) purports to clarify the scope of what would constitute an ordering institution by excluding most value transfers that are done incidentally to the provision of another service, unless the ordering institution is a:

- a financial institution (63A(4)(a)(i)),
- a business providing an international value transfer service incidentally to a designated service covered by item 50, 50A or 50B of table 1 in section 6 (63A(4)(a)(ii)), or

[5] The AML/CTF Act currently states *financial institution means:*
(a) an ADI; or
(b) a bank; or
(c) a building society; or
(d) a credit union; or
(e) a person specified in the AML/CTF Rules.
The AML/CTF Rules made under paragraph (e) may specify different persons to be financial institutions for the purposes of different provisions of this Act.

- a business providing an international value transfer service incidentally to a gambling service (contained in table 3 of section 6) (63A(4)(a)(iii)).

The FSC submits that the use of the wording "unless the ordering institution is a financial institution" potentially causes confusion and that the definition of "financial institution" currently used in the AML/CTF Act should be clearly set out in this section of the EM to provide greater clarity. The EM at paragraphs 607 and 611 also refer to these subsections but do not clarify the position[6].

The FSC **recommends** that the Bill and EM should make it clear that these obligations (including reporting) are intended to apply to payment service providers only, including banks, remitters and other types of payment service providers (i.e. those providing a value transfer designated service).

Yours sincerely,

Ashley Davies
Policy Director – Legal

[6] The FSC acknowledges that the EM provides some guidance at paragraph 615 "when considering if a transfer is incidental to the provision of another service, the question to consider is whether the other service is a type of value transfer service, in which case it is irrelevant to consider whether the value transfer is incidental. However, if the other service is of a different nature (for example, managing a fleet of cars), then the transfer of value will be excluded." However, it is suggested that further guidance is provided.