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 Sir/Madam

Anti-Money Laundering and Counter-Terrorism Financing Amendment Bill 2024

The Australian Financial Markets Association (AFMA) represents the interests of over 130 participants in Australia's wholesale banking and financial markets. Our members include Australian and foreign-owned banks, securities companies, treasury corporations, traders across a wide range of markets and industry service providers. Our members are the major providers of services to Australian businesses and retail investors who use the financial markets. A significant proportion of AFMA's members are reporting entities for the purposes of the AML/CTF Act.

We are pleased to provide a submission to Committee's inquiry into the *Anti-Money Laundering and Counter-Terrorism Financing Amendment Bill 2024*.

Executive Summary:

AFMA notes the following, by way of executive summary:

- AFMA supports the passage of Bill and the continued simplification and modernisation of Australia's AML/CTF legislative framework to reduce ambiguity, promote international alignment and support reporting entities in frustrating serious financial crime;
- It is imperative that there is a legislated assisted compliance period of an eighteen-month duration, commencing on the finalisation of the Rules;

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- The Bill needs to align the penalties for breaches of AML/CTF programs to the seriousness of the infraction;
- The customer due diligence requirements for reporting entities should be less prescriptive and allow reporting entities to conduct customer due diligence in accordance with the risk-based approach;
- The amendments to the tipping off offence should expressly permit the sharing of information with offshore related entities and internal/external auditors;
- The definitions of "reporting group" and "business group" should expressly accommodate inbound corporate structures so as to include offshore related entities and other parts of the legal entity operating in other jurisdictions;
- There should be no additional Australian obligations of a reporting entity providing a designated service through an offshore permanent establishment where the offshore jurisdiction is not materially deficient from a FATF perspective;
- The commencement for the value transfer changes should be deferred to align with the commencement of the IVTS reporting framework; and
- The keep open notice amendments should be refined to remove foreign offences and increase the threshold to imprisonment for three years. In addition, the defence for reporting entities should be aligned with the current Chapter 75.

Commitment to Simplification & Modernisation

AFMA remains committed to the Government's proposal to simplify and modernise Australia's AML/CTF legislative framework. Our members have engaged extensively with both the Attorney-General's Department (**AGD**) and AUSTRAC regarding ways in which the AML/CTF regime could be enhanced to assist with the frustration of serious financial crime and to promote alignment with the regimes in other jurisdictions.

Any prospect of Australia being grey-listed by the FATF would significantly hinder Australia as a location to conduct financial business and undermine confidence in Australia's financial markets. AFMA supports the Government in undertaking legislative action that is necessary to ensure that grey-listing does not occur. On this basis, AFMA reiterates its support for Tranche Two entities being brought within regulatory scope.

AFMA supports the passage of the legislation. While it is our hope that the legislation may be improved through the Committee's Inquiry, as set out below, our suggestions should not be inferred as a lack of support for the Bill. To the extent that the suggestions below are not ultimately incorporated into the final legislation, then AFMA will continue to seek enhancements through consultation on the development of the Rules and AUSTRAC guidance.

Approach to AML/CTF Simplification & Modernisation

AFMA and its members reiterate the following principles that should underpin the reform process and the design of Australia's AML/CTF legislative and regulatory framework:

- Articulation of core requirements only in the Act with additional granularity and detail in the Rules;

- Restoration of the primacy of the risk-based approach, with as little prescription within the Act and Rules as is permissible to achieve/maintain FATF compliance;
- Minimisation of regulatory duplication through deference to processes undertaken in other jurisdictions, to the extent that these jurisdictions have AML/CTF frameworks that are not materially deficient from a FATF perspective;
- Clear articulation of legal obligations that minimise ambiguity and the necessity for reporting entities to obtain independent legal advice on matters of interpretation; and
- The continuation of existing exemptions so as to not increase the regulatory burden for entities that currently benefit from those exemptions, with these exemptions being contained in the Rules to ensure that they remain current and fit-for-purpose.

Commencement, Transition and Proposed Regulatory Approach

AFMA's primary concern with the provisions of the Bill is the timeframe for commencement. With the exception of the requirements for reporting value transfer instructions, the commencement for the changes in the Bill is 31 March 2026. This may be a little more than twelve months from the Bill attaining Royal Assent. For regulatory change of this magnitude, AFMA would expect an implementation timeframe of a minimum of eighteen months and hence, for existing reporting entities, the timeframe for commencement is insufficient.

This concern is exacerbated by the fact that much of the granularity in terms of reporting entity obligations will only be provided in the Rules and will be supplemented by AUSTRAC guidance. AFMA understands that the process for commencement of substantive consultation on the Rules will only occur once the Bill receives Royal Assent and, given the extent to which the Rules will require refinement given the scope of the legislative changes, AFMA anticipates that the consultation on the Rules will be extensive and will take a number of months. This means that, practically, the final legislative framework (encompassing both the Act and the Rules) may only be finalised less than six months prior to the commencement time.

The other complicating factor for reporting entities is the fact that the Bill and Explanatory Memorandum were not consulted on in exposure Draft form, which prevented reporting entities from being able to anticipate and influence proposed changes.

As noted above, AFMA supports the lack of prescription in the Bill (with the exception of the Customer Due Diligence requirements, as noted below) and believes that the provisions in the Bill should remain high-level and principles-based. However, given the extensive consultation that will be required on the Rules, it is appropriate that the legislation include a mechanism whereby current reporting entities are not exposed to enforcement action from regulators for a reasonable period while they undertake best endeavours to operationalise the new requirements.

AFMA understands that when the AML/CTF Act was introduced in 2006, a commencement date of eighteen months from the date of Royal Assent was augmented by a direction from the Minister that the AUSTRAC CEO not take compliance action for three years from the commencement date. AFMA believes a similar approach is appropriate in relation to the changes included in the Bill and believes that this compliance approach should be specifically included in the legislation.

AFMA acknowledges that the timelines for commencement are being driven, in part, by the timetable for the next mutual evaluation of Australia by FATF. On this point, our view is that the key priorities of FATF arising from the last evaluation, namely bringing Tranche Two entities within scope and expanding the scope of designated services to include services in respect of digital assets, may be prioritised from a timeline perspective without adversely impacting existing reporting entities and their businesses.

In summary, AFMA believes that a direction from the Minister, to be included in the legislation, that the AUSTRAC CEO not to undertake enforcement action against reporting entities who are undertaking best endeavours to comply with the new requirements for a period of eighteen months is appropriate, and that this period commence on the date that the Rules are finalised.

AML/CTF Programs

Under the provisions in the Bill, all reporting entities are required to have an AML Program, which consists of the reporting entity's ML/TF Risk Assessment and the AML/CTF Policies.

The AML/CTF Policies include policies, procedures, systems and controls to appropriately manage/mitigate risk and ensure compliance. These need to be appropriate based on the nature, size and complexity of the reporting entity's business and need to be updated every three years or a time prescribed by the Rules, whichever is the earlier. The Bill stipulates the issues that need to be addressed in the AML/CTF Policies.

AFMA's concern is that, given the "AML/CTF Policies" is defined to include policies, procedures, systems and controls, then any breach of operating procedures or policies, no matter how minor, will be taken to be a breach of the AML/CTF Program and accordingly will be subject to the same penalties as a systemic breach. This issue is currently addressed through the delineation between Part A and Part B of the AML/CTF Program; however, given no such delineation is proposed in the Bill, then the legislation needs to ensure that potential penalties are calibrated to the seriousness of the infraction.

In addition, AFMA supports the clarification of proposed Section 29B to ensure that senior managers are not required to approve all changes to low level, operational policies, regardless of the materiality of the change, in a manner that is consistent with the reporting entity's risk-based approach.

Customer Due Diligence

A key principle of AML/CTF simplification and modernisation is that there is less friction in the provision of a designated service. However, our view as to the requirements in the Bill will be that they may, in many circumstances, delay the provision of the designated service relative to the status quo.

This view comes from the requirement under the Bill that, prior to the provision of the designated service, a reporting entity will need to be satisfied "on reasonable grounds" a number of elements, including, relevantly, whether the customer is a politically-exposed person (**PEP**) or a person designated for financial sanctions. In order to be satisfied "on reasonable grounds", it is necessary that the reporting entity collect and verify information confirming the element.

Under current processes, particularly in a retail context, reporting entities are able to confirm certain matters, such as PEP screening and or financial sanction designation after the provision of the designated service. AFMA notes the existence of the exemption in proposed Section 29; however the current equivalent of this exemption is used sparingly and would not be relied upon in a business-as-usual context.

AFMA's view is that the customer due-diligence requirements should be less prescriptive and allow reporting entities to manage the ML/TF risk of their customers or customer types using a risk-based approach that permits the provision of the designated service prior to the establishment of all of the elements in proposed Section 28 or application of simplified due diligence, given that appropriate remediation can occur should all of the elements not be established.

Tipping Off

AFMA broadly supports the proposed amendments to the tipping off offence from the perspective that the amendments will enhance the ability of reporting entities to share information with their related entities and other reporting entities to properly frustrate financial crime. However, AFMA believes that the Bill should be refined to address the following circumstances:

- The Bill should expressly permit the sharing of information with both internal and external auditors that may not be part of the reporting/business group, such as through clarifying that such sharing would not reasonably be expected to prejudice an investigation. This is consistent with FATF recommendations and should expressly be permitted in the enabling legislation;
- Coupled with amendments to the definition of "reporting group" as suggested below, the Bill should expressly permit the sharing of SMR information with offshore entities, particularly given that such entities may have a role to play in the Australian reporting entity complying with AML/CTF obligations. This approach would be consistent with FATF Recommendation 18. The Rules would be able to stipulate any jurisdictional limitations associated with the sharing of the information.

The latter point is a priority issue for AFMA. It is vitally important that Australian reporting entities are able to share information with related parties offshore and that the interaction between the amendments to the tipping off offence (which facilitate the sharing of information within reporting groups) and the reporting group definition acknowledge that Australian reporting entities may be headquartered offshore and may operate within the same legal entity as their parent.

Given the tipping off changes are largely beneficial to reporting entities, AFMA submits that the commencement of the provisions should be brought forward to 28 days from Royal Assent.

Reporting Groups

AFMA welcomes the proposed amendment in the Bill that allows for non-reporting entities to be included in business groups and, accordingly, reporting groups.

However, we remain concerned that the proposed definition of reporting groups does not properly address in-bound corporate structures, where the ultimate parent and related entities may be offshore. On our reading of the proposed amendments, the automatic business group definition will

only apply where the ultimate controlling entity resides in Australia, which would mean that inbound reporting entities would be required to make an elective business group, which is not what we understand the policy intention of the legislation to be. In this regard, we note that where the Australian reporting entity is the same legal entity as the parent entity, such as in the case of a foreign bank branch, then the concept of "control" in proposed Section 10A does not apply.

On this basis, the Bill/Explanatory Memorandum should ensure that the definitions of "reporting group" and "business group" can accommodate inbound corporate structures, such that Australian reporting entities are able to share information with their offshore ultimate parent entities and related entities.

Foreign Branches/Subsidiaries

AFMA notes the statutory construction in relation to the provision of designated services at or through a permanent establishment in a foreign country ("offshore permanent establishment" or "OPE") is that the reporting entity will need to be satisfied of certain high-level criteria, with additional obligations being imposed where the designated service is being provided from an Australian permanent establishment.

We understand that the policy basis for this approach is to reduce regulatory duplication between the AML/CTF regimes of other jurisdictions (such as the jurisdiction from where the designated service is being provided) and Australia in circumstances where the other jurisdiction's AML/CTF regime is not materially deficient. Where such a regime is materially deficient, such that the high-level criteria cannot be satisfied, an obligation sits with the reporting entity to notify AUSTRAC where adherence to the Australian obligations could not be permitted in the offshore jurisdiction.

AFMA's primary concern with the proposed approach to foreign branches/subsidiaries is that, in respect of the provision of a designated service from an overseas jurisdiction, the reporting entity will be required to establish all of the elements in relation to customer due diligence that are required under proposed Sections 28(1)-(3). This may also be exacerbated by the new AML/CTF Rules or guidance (yet to be seen) if CDD prescription is tied to Sections 28(2)-(3), which then may inadvertently capture OPEs.

Further, as noted above, AFMA is of the view that the establishment of each of the elements on reasonable grounds prior to the provision of the designated service is overly prescriptive in an Australian context; this concern is even more pronounced in relation to the provision of a designated service from an overseas branch or subsidiary with no nexus to Australia. The proposed approach will require entities to essentially map the CDD requirements for the offshore jurisdiction to the Australian requirements and potentially add Australian-centric processes offshore. In addition to mapping legislation, different jurisdictions may interpret requirements differently by way of guidance or regulatory expectations, which adds significant complexity when attempting to apply an Australian regulator's expectations to the same or substantially similar obligation where there is no nexus to Australia. This will both increase regulatory duplication and undermine the competitiveness of the overseas branch or subsidiary. This is contrary to the policy intent of simplification. A defence should be available where the laws of the foreign jurisdiction give substantive effect to the relevant Australian requirements.

AFMA supports the retention of the current exemption that allows the provision of a designated service through an offshore branch or subsidiary without reference to the majority of the Australian requirements (in particular CDD requirements), in circumstances where the offshore jurisdiction is not materially deficient from a FATF perspective.

Value Transfer

While AFMA appreciates the extension of the changes to the reporting requirements for value transfers to the date of proclamation, given the exceptionally significant operational burden arising from the proposed changes, our view is that the value transfer changes more generally is an area where significantly extended implementation timelines are warranted.

Financial institutions are currently focusing SME resourcing on implementing changes to systems due to the adoption of ISO20022, with the finalisation of the adoption being targeted as November 2025. This limited implementation timeline for IVTS would require reporting entities to refocus payments SME resources to these new reporting requirements adding risk to the delivery of both the ISO20022 and IVTS frameworks in relation to value transfers, including the inclusion of necessary information.

In addition, the hierarchies that need to be applied to determine whether an institution is an ordering, intermediary or beneficiary institution in proposed Section 63A are complex and bespoke to Australia, requiring additional clarity through Rules and AUSTRAC guidance.

Given the complexity of the proposed changes in relation to value transfers and the fact that much of the detail will be included in Rules and associated schema, AFMA's view is that the timing for commencement of Schedule 8 of the Bill should reflect the commencement of the new IVTS reporting framework, which is when reporting entities and AUSTRAC are able to update or implement required system changes.

Keep Open Notices

AFMA notes the proposed amendments in relation to keep open notices. We have previously expressed concern regarding the removal of AUSTRAC approval in relation to keep open notices, due to significant concerns from our members that this will result in a considerably higher number of notices being issued to our members, thereby exacerbating compliance costs.

To this extent, AFMA suggests an amendment to the definition of "serious offence" in proposed Section 39B to an offence that is punishable by imprisonment for 3 years or more, together with the removal of foreign offences under proposed Section 39B(2)(b). These amendments should reduce the operational burden and compliance risk associated with the proposed changes.

AFMA also is of the view that the exemption in proposed Section 39D(2), that is, the ability for the reporting entity to continue to conduct initial, ongoing and enhanced due diligence and to continue to apply AML/CTF policies, should be broader to align with the current exemption in Chapter 75 of the Rules.

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Yours sincerely,

Rob Colquhoun
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Head of AML