SENATE LEGAL AND CONSTITUTIONAL AFFAIRS COMMITTEE
QUESTIONS ON NOTICE TO ATTORNEY-GENERAL'S DEPARTMENT

RESPONSE TO QUESTIONS ON NOTICE
BY SENATOR LUDWIG

Senator Ludwig asked the following questions:

1. Re Clause 6, table 1, items 6 & 7 refer to a "loans business", but this is not defined in Clause 5 definitions. Question arises - is a loans business:
   a) any business that conducts a loan, or
   b) a business that provides loans in the course of business, or
   c) a business in which loaning forms a significant part of the business, or
   d) a business in which loaning forms the substantial part of the business.

   On the same point - the EM states that it is to decide whether the practice of making loans is "core activity" - it then uses the example of Centrelink and states it "is not in the business of loan making". That is not true - see Pensions Loans Scheme, also drought assistance. Where does that leave Centrelink?

   In addition, where does HECS/HELP fit into this schema?

Response: Loans business is a business which has as a core or significant or primary part of its business activities the provision of loans. It is a definition to be applied to the facts of the whole business activity. In addition the term "business" is defined in clause 5 of the bill to include "a venture or concern in trade or commerce whether or not conducted on a regular repetitive or continuous basis".

The EM clarifies that the Pension Loan Scheme operated by Centrelink is not a designated service for the purpose of the Bill. In addition Centrelink would not fall within the definition of the term 'business' in clause 5 of the bill.

2. Re Clause 6, table 1, item 9 refers to a "forfaiting business", but this is not defined in Clause 5 definitions.
   a) Therefore the same questions in Question 1 a) to d) hold in regards forfaiting businesses - please answer accordingly with regards to forfaiting businesses.
   b) Is forfaiting a subset of factoring? If forfaiting is taken to be a subset of factoring (which is defined) then why list it separately at all?
   c) The EM seems to weave between spelling this practice as "forfaiting" and "forfeiting" which is correct, and if both are, which will the department adopt for the sake of consistency?

Response (a): the term 'forfaiting' is not defined in clause 5 because it has its ordinary commercial meaning. It is an understood principle of statutory interpretation that a word will have its ordinary meaning unless supplanted by a statutory definition.

The explanatory memorandum on item 9 which uses the term is as follows

"**Item 9 - forfaiting** - this item covers forfaiting a bill of exchange or a promissory note in the course of carrying on a forfaiting business. The item implements footnote 6 of paragraph 2 of the FATF Glossary definition of *financial institution.* (The Australian Dictionary of Banking and Finance, published by Law Book Information Services in 1997, defines forfaiting as *a fixed interest trade financing technique whereby an exporter who receives a term bill of exchange or promissory note for the supply of goods and services discounts the bills with a financial instiltution (the forfaiter) after having accepted the bill on a without recourse basis. In doing so the exporter passes all risks and responsibility for collection to the forfaiter in exchange for immediate cash payment. Forfaiting is common in European trade*) The customer is the person whose bill or note is forfaited."

As with the answer to question 1 forfaiting would need to be a significant part of the business concerned and whether or not it is a forfaiting business would be determined by reference to the whole of the business activity.

(b) The term 'factoring a receivable' is used in item 8. The term 'factoring' is defined in clause 5.

The two items of "factoring" and "forfaiting" are separate because 'factoring' relates to receivables and 'forfaiting' relates to bills of exchange and promissory notes.

The explanatory memorandum for the clause 5 definition of factoring is as follows:

***factoring* –** the definition leaves the term to be read according to its ordinary meaning. The definition also provides that the term includes anything that under the regulations is taken to be factoring for the purposes of the Bill. This will enable regulations to be made to capture activity designed to circumvent obligations under the Bill. The words *is taken to be* are intended to extend the ordinary meaning. The definition is not affected by any other definition in the Bill. The term refers to the practice whereby a 'person' (a legal or a natural person), the factor, advances money to another person in exchange for taking on that person's debts.

The explanatory memorandum on item 8 is as follows:

Item 8 – factoring a receivable - this item implements paragraph 2 (see footnote 6 to paragraph 2 of the FATF Glossary definition of financial institution) – see also explanatory memorandum to definition of term *factoring* in clause 5. The customer is the person whose receivable is factored. (The Australian Dictionary of Banking and Finance, published by Law Book Information Services in 1997, defines a receivable as *claims held against customers and others for money, goods or services*)

(c) Forfaiting is a commercial term as described above. Forfaiting has its ordinary meaning. The different usage refers to different activities.

3. Re repeated definition of "consumer" in Clause 6 Table 1, is there any reason why, for simplicity's sake, the definition of consumer could not be moved to Clause 5?

Response: the term 'consumer' is not used in clauses 5 or 6. However the word 'customer' is defined in clause 5 with reference to clause 6. The purpose of the tables in clause 6 is to precisely identify services/activities for which the provider will become a reporting entity with obligations under the Bill. The purpose of identifying the customer in each item in the tables is for the purpose of ensuring that reporting entities identify that person before providing the designated service.

4.

a) Regarding the explicit differentiation of accounts held by trustees, building societies and credit unions as opposed to general account providers, why is this necessary?

b) Re Clause 6, table 1, and the difference in construction of Items 15 (where an 'account provider' is referred to) and 18 (where one is not), is this intentional? If it is, then why are Items 16 and 17 necessary?

Response;

a) This is necessary because of the different legal status of these entities. It is necessary to identify the legal entity to be able to define the nature of the service the particular entity can provide

b) Item 15 is drafted to take account of the fact that a building society etc cannot provide cheque accounts itself but may be able to provide a cheque facility whereby a customer can draw a cheque on an account held by the building society etc.

The same comment applies to Item 16 whereas item 17 designates a very different service (the difference from item 15 being that the ADI etc is the issuer of the instrument against itself (eg where a bank issues a bank cheque to a person who presents at a bank with the money but does not have an account with the bank) rather than being the provider of a facility which enables a

customer to draw a cheque on an account provided by a third party. Item 15 can be grouped with item 19 because the legal status of the provider is the same in both items. Similarly items 14 and 18 and 16 and 20 can be grouped together.

5. Regarding Clause 5 - why has no proper definition of 'issuing authority', 'issuer' or 'issuer' been given, as is the case with other Acts, and does this have any effect on whether (for example) a traveller using traveller's cheques would be conducting a designated service under clause 6 table 1 item 25.

Response: These terms are not defined because they have their ordinary meaning. The Bill does not provide a dictionary of all terms used in it. A traveller using a traveller's cheque to pay for goods or services or to obtain currency is not issuing the traveller's cheque and would not be conducting a designated service.

6. For the sake of simplicity, clarity and ease of use, why is there a number of definitions that appear outside the definitions section, and why can't they be moved there? See also Question 3.

Response: Where terms in clause 5 are defined by reference to other clauses in the Bill which in turn are wholly devoted to defining the term this is generally because the term in fact represents a more complex concept. This is a common drafting technique.

7. In regards to the KYC regime in Part 2 Division 2 - is the exemption broad enough to include a circumstance where an existing customer was seeking to access a different designated service for the first time (i.e. in this way you would eventually reduce the number of non-CDD compliant existing accounts by attrition)? Wouldn't it be desirable in such instances to get the reporting entity to do the KYC test at that point?

Response: The exemption covers the provision of any designated service to an existing customer. However, if the customer in accessing a new designated service presented a different increased risk, as part of ongoing due diligence obligations the reporting identity may need to verify the identity of the person. For example a bank has an existing customer who has conducted low level transactions on their account over a period of time (item 3 of table 1). The customer then requests the same institution to sell him a significant amount of shares in a company (item 35). The cost of the shares is demonstrably inconsistent with the customer's existing profile. This scenario would trigger a suspicious matter reporting obligation under clause 41 and the financial institution would be required to take action, including possibly verification of the customer's identity under clause 29.

8. With regards to the EM description of clause 28 "Scope" on page 74 - is this in error, and if not, what does it mean?

Response: This is not an error. The EM is using the same sub-heading used in the clause itself. Subclause 28(1) defines the category of services, described as post-commencement designated services which are exempt from cl.32 and 34.

9. With regards to Table 1 in the EM, can the Department please provide a copy of the table showing what levels of compliance it estimates will be reached as a result of passage of this legislation (assuming no further amendments)?

Response: Table 1 reflects the assessment of the FATF of Australia's current level of compliance. FATF's compliance assessment is not just about the legislation as it involves an assessment of the effectiveness of the legislation. Further, the FATF methodology for addressing compliance is extensive. Completion of Australia's Mutual Evaluation required a 2 week onsite visit by a team of 6 evaluators and several months of information gathering and analysis. The Bill, however, will significantly improve Australia's overall level of compliance.

10. In regards clause 6(7) is it the case that behaviour which is non-criminal could effectively be criminalised via simple regulatory addition to the table? Can the Department please provide any other examples of legislation where this is so

Response: No. The bill does not criminalise the provision of designated services. It provides certain regulatory obligations, which must be met where certain services are provided. Failure to meet those regulatory obligations can lead to civil or criminal penalties.

The following is the text of the response to the question on notice of 15 November which outlines the purpose and intent of subclause 6(7):

> Subclause 6(7) is designed to provide a means to amend an item in a table in clause 6 in circumstances where new products of a similar kind to the existing designated services are created or structured in such a way that they would not be covered by existing items in the tables or where an industry or sector identifies and attempts to exploit a loophole in the table. Regulations will be disallowable instruments and subject to the normal procedures under the *Legislative Instruments Act 2003.*