CHAPTER 3

KEY CONCERNS FOR INDUSTRY

3.1 Business and industry bodies who participated in the committee's inquiry expressed in-principle support for the need for an effective and efficient framework to prevent money laundering and terrorist financing activity in Australia. However, a range of concerns emerged in submissions and oral evidence in relation to specific aspects of the proposed AML/CTF regime. These included timing issues with respect to consultation and implementation of the new regime.

3.2 This chapter considers the key issues and concerns for industry raised in the course of the committee's inquiry.

Consultation process

3.3 On 16 December 2005, the Minister released the Exposure Bill for public comment for a period of four months, with the aim of introducing the legislation into Parliament in June 2006.[1] As noted in Chapter 1, submissions to that process close on 13 April 2006. However, the committee understands that extensive consultations in relation to the AML/CTF regime have been progressing on an ongoing basis with the financial sector since January 2004.

3.4 Key features of the consultation process aside from the release of the Exposure Bill have included:

- commencing in July 2005, a series of four Ministerial meetings between the Minister, officials from the Department and AUSTRAC, and representatives of the financial sector; and
- the later establishment of a formal consultative framework comprising of:
    - an overarching ministerial advisory group (that is, the Minister and representatives of the peak industry bodies); and
    - a number of joint industry/AUSTRAC technical working groups and sub-working groups.[2]

3.5 The committee understands that there are currently four working groups reporting to the ministerial advisory group, each of which is co-chaired by industry representatives and government. In three cases, the government co-chair is AUSTRAC and in the other case, the co-chair is the Department. These working groups are examining the following areas:

- AML/CTF programs;

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1 See http://www.ag.gov.au/aml (accessed 7 February 2006)

2 *Committee Hansard*, 14 March 2006, pp 63-65.

- international issues;
- risk principles; and
- identity verification.[3]

Timeframe for consultation

3.6 During the course of the inquiry, the committee learned that most industry groups have been largely satisfied with the extent and nature of their ongoing engagement with the Minister and/or the Department in terms of preliminary discussions and a consultation process.

3.7 However, despite this, all industry groups expressed concern that the four-month consultation period for the Exposure Bill itself, and the associated Rules and Guidelines, is not adequate to thoroughly assess the full impact of the regime.

3.8 The Investment & Financial Services Association (IFSA) argued that this is amplified by the fact that key areas of the regime are yet to be finalised. At the time of IFSA's submission:

> … around half of the consultation period ha[d] passed and much of the detail around critical elements of the package such as an acceptable method for Electronic Verification; acceptable methods for determining P[olitically] E[xposed] P[erson]s; Risk Triggers for re-identification; Continuity of Relationship and Low Risk Designated Services are still outstanding.[4]

3.9 IFSA also pointed out, despite the best efforts and intentions of all parties, adequate consultation on a finalised package in the remaining timeframe is not possible:

> … the range of services covered in the Bill are very broad and in order to effectively regulate those services, the relevant products themselves and the way they operate and are distributed needs to be clearly understood. For this reason, industry believes that effective consultation on the AML/CTF package needs to be iterative (i.e. submissions made by industry, considered by AUSTRAC, AUSTRAC then providing feedback or seeking further clarification from industry or both, and industry responding, etc).[5]

3.10 Mr John Anning from the Financial Planning Association of Australia (FPA) agreed with this assessment:

> Given the scale of the task to create an effective AML CTF regime, it is not an indictment of the effort put in by all parties that much remains to be done before industry can comment definitively on the proposed regime. FPA strongly believes therefore that the government should extend the

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3 *Committee Hansard*, 14 March 2006, p. 65.

4 *Submission 2*, p. 2.

5 *Submission 2*, p. 2.

> consultation period beyond the current deadline of 13 April in order for comprehensive analysis to be undertaken as to how the components of the regime will work together. The effective implementation of this legislation is too critical to Australia's welfare to be jeopardised by strict adherence to initial time lines.[6]

Staggered release of Rules

3.11 Many submissions and witnesses argued that the timeframe for consultation was particularly inadequate given that the majority of the Rules were not released as part of the consultation process, and particularly since much of the detail forming the basis of the new regime is to be included in the Rules and the Guidelines.

3.12 Many submissions expressed concern that, without the full package of draft legislative instruments, affected bodies are unable to analyse to a sufficient extent the true impact of key areas of the regime, the practicalities of implementation, and whether or not the regime will achieve the desired objective of countering money laundering and terrorist financing.[7]

3.13 As IFSA explained:

> … the staggered release of the draft Rules, which form a fundamental part of the regime, makes it extremely difficult to undertake comprehensive analysis and provide carefully considered comments to Government.[8]

3.14 The ABA argued that the banking industry holds serious doubts that the April deadline can be met at the present pace:

> The consultative framework set up by the Minister is workable but the issues are very complex, there are many uncertainties in the existing drafts, and progress is slower than expected.
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> …
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> The industry concern is that if the AML legislative package is pulled together in a rush to meet the current mid-April deadline, issues will not be properly resolved, or will be overlooked, resulting in implementation difficulties and ongoing operational problems.[9]

3.15 The ABA submitted further that at least five or six weeks would be required from the date of delivery of the complete AML/CTF package in order to conduct a complete analysis and to prepare detailed submissions to the Department's consultation process.[10]

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6 *Committee Hansard*, 14 March 2006, p. 16.

7 For example, IFSA, *Submission 2*, p. 2; ING Direct, *Submission 13*, p. 2.

8 *Submission 2*, p. 2.

9 *Submission 18*, p. 2.

10 *Submission 18*, p. 2.

3.16 In their joint submission, CPA Australia and The Institute of Chartered Accountants in Australia noted that a four month timeframe for comment would normally be adequate but, since 'the majority of the related rules and guidelines, which provide the detail on compliance processes and obligations, have not yet been released' there is simply not enough remaining time.[11]

3.17 Mr John Anning from the FPA made a similar argument:

> At the moment it is impossible to take a definitive position on the draft package, given that so much of it is unknown. Currently, you cannot make sense of the draft bill until you see the subsidiary pieces. If the draft bill contained all the relevant principles—the key one which is missing for us at the moment is appropriate recognition of the risk based approach to implementation—it would be possible to comment properly on the bill itself rather than wait for the rules and guidelines.[12]

3.18 Ms Michelle Mancy from American Express supported this view:

> In view of the fact that the law is not yet complete, the April deadline for completion of the consultation processes is too short. Even if all the missing rules are released in the next two to three weeks, it would not be enough time for organisations to absorb impact and effectiveness before responding in a meaningful way. I will give you an example of how the job has only been half done to date. As you are well aware by now, identification comes in two parts: collection and verification. We have draft rules for collection but nothing for how it is to be verified. This area is one of great financial burden to institutions, and we are 50 per cent incomplete on the information relevant to assess whether we can do it at all and how much it will cost.[13]

3.19 Insurance Australia Group (IAG) submitted that it would be prudent for the consultation period to be reassessed based on industry having access to the complete suite of initiatives contained in the reform package.[14]

3.20 In its submission, The Treasury supported the availability of the complete package of reform proposals:

> Treasury's experience in implementing broad-ranging financial sector reform, such as the *Financial Services Reform Act 2001* (FSR Act), has demonstrated that the availability of a full package of reform proposals is desirable to allow industry to understand the range of requirements under which they are placed and thereby ascertain their compliance costs and necessary system and personnel changes. Given this, it would be desirable for industry to have the opportunity to comment on the full package of

11 *Submission 7*, p. 1.

12 *Committee Hansard*, 14 March 2006, p. 20.

13 *Committee Hansard*, 14 March 2006, p. 48.

14 *Submission 11A*, p. 8.

> AML/CTF measures. To date we note that significant obligations are yet to be specified in rules and provided to industry for their consideration.[15]

Department response

3.21 At the hearing, the Department responded to concerns raised with respect to the consultation process. A representative from the Department told the committee that the consultation period is 'genuine' and, from its perspective, 'a very positive exercise'. He stressed that the Department has taken, and will take, comments and criticisms 'on board'. In particular, he noted that:

> People obviously have to speak about the exposure draft which is out there, but I can guarantee that the final bill, even if nothing else happened from here on, would be different in a whole lot of respects from what we have here. That, of course, is part of the process and makes it a bit difficult for people to comment on, and we have the difficulty in, firstly, making announcements about changes that will be made, because it will be a government decision—it is not up to us as officers to make that call—and, secondly, because the consultation period is not over. It is possible that things will change; people will come up with good ideas that we will be more than happy to take on board. Some of the evidence given this morning was that comments have been made, they have sat on the table and not been reacted to. From our perspective, that is not the way the process is working.[16]

3.22 In relation to concerns about the large number of Rules yet to be released for comment during the consultation process, the representative assured the committee that 'the key rules, the vital rules, the rules needed to make it work'[17] would be released prior to the end of the consultation period. He told the committee that this amounts to 'five sets' of Rules, that is:

- AML/CTF Programs Rules ;
- Identity Verification Rules;
- Suspect Transaction Reports Rules;
- Correspondent Banking Rules; and
- Threshold Reporting Rules.[18]

3.23 He noted that, 'the position is [not] quite as bleak as some of the evidence has suggested', and that, of those sets of Rules:

> AML programs are at a very advanced stage, suspect transaction rules are at a very advanced stage, and I think threshold reporting is too. The real work

15 *Submission 29*, p. 2.

16 *Committee Hansard*, 14 March 2006, p. 61.

17 *Committee Hansard*, 14 March 2006, p. 61.

18 *Committee Hansard*, 14 March 2006, p. 61.

> that has to be done is in ID verification rules and the correspondent banking rules … The current approach being taken in relation to both of those rules is to create a further version of them based on the risk based approach, and that will be presented to industry over the next short period. We hope that we will be able to produce draft ID verification rules in time for the next meeting of the ministerial advisory group on Thursday. I think correspondent banking rules will take a little longer because we are still getting information. They are going to be drafted in consultation with industry.[19]

3.24 AUSTRAC's legal representative advised that there are 'essentially three broad categories of outstanding rules', namely in relation to identification, reporting obligations and 'a miscellaneous category of definitions and the like'. She told the committee that the process with respect to release of these Rules to the working groups is about two weeks behind schedule.[20]

3.25 In relation to the possibility of opportunities for an extended period of consultation or further consultation prior to finalisation of the Exposure Bill and its introduction into Parliament, the departmental representative noted that:

> It is really the minister's call as to whether there is that further period of consultation or further opportunities for industry to examine the bill, so I cannot make any commitment in relation to that. At this stage the minister is still keen to introduce legislation as soon as it can be done. Bearing in mind the length of time that this process has taken, we are very keen to push on. We have now been evaluated by FATF and 12 months after the evaluation we are going to be called upon to explain progress, so there are time pressures which people should not lose track of.[21]

Timeframe for implementation

3.26 Many industry and business entities raised the issue of a timeframe for implementation of the new regime. There was widespread uncertainty about the Federal Government's plans for implementation of the Exposure Bill, particularly given the Exposure Bill's scope and complexity. Many submissions and witnesses noted the extensive obligations imposed by the Exposure Bill and the anticipated costs of administration and compliance, including implementation of appropriate information system changes, which would be particularly burdensome for small- and medium-sized enterprises.[22]

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19 *Committee Hansard*, 14 March 2006, p. 61.

20 *Committee Hansard*, 14 March 2006, p. 78.

21 *Committee Hansard*, 14 March 2006, p. 61.

22 For example, IFSA, *Submission 2*, p. 2; CPA Australia & The Institute of Chartered Accountants in Australia, *Submission 7*, pp 1 & 4; Insurance Australia Group, *Submission 11A*, p. 8; Suncorp-Metway Limited, *Submission 14*, p. 4, Platinum Asset Management, *Submission 21*, p. 3.

3.27 The majority of industry groups were of the view that a period of two to three years would be necessary for implementation. However, the committee notes that the Minister has indicated that a period of 12 months to comply with the legislation is more likely.[23]

3.28 Mr Tony Burke from the Australian Bankers' Association (ABA) told the committee:

> Once the legislation is ready, we believe that a time of two to three years will be necessary to implement this very complex piece of legislation which has very significant ramifications across our institutions. At this stage we do not have a firm position from government as to what they see the transition period as being, but it is our firm view that regardless of where the drafting ends up, a time of two to three years will be necessary.[24]

3.29 Mr Raj Venga from the Australian Association of Permanent Building Societies agreed:

> Our initial view is that we will need two to three years to properly implement the proposed legislation, given the systems modifications, staff training and processes that need to be undertaken. We note that the FSR provided a transition period of two years, which I thought was a reasonable indication of the time required, because the AML is no less difficult to implement than the FSR.

3.30 IFSA submitted that the AML/CTF regime is 'one of the most significant reforms to the financial services industry in the last twenty years'.[25] It also drew comparisons with the consultation and transition periods relating to the FSR regime, noting that they amounted to a combined total period of six years:

March 1999:	CLERP 6 Consultation Paper released
February 2000:	Draft FSR Bill released
September 2001:	Bill receives the Royal Assent
March 2002:	Legislation commences with 2 year transition period
March 2004:	End of transition period[26]

3.31 Further, and importantly, IFSA pointed out that:

> … despite the extensive consultation … industry and Government are still attempting to overcome a number of practical difficulties with the FSR regime. Indeed, while many of the ongoing difficulties were largely unintentional, IFSA nevertheless believes that the industry's and the

23 S. Patten, 'Laundering laws rinsed off', *Australian Financial Review*, 17 March 2006.

24 *Committee Hansard*, 14 March 2006, p. 2.

25 *Submission 2*, p. 2.

26 *Submission 2*, p. 3.

> Regulator's experience would have been far worse had there not been extensive consultation from the outset.[27]

3.32 Suncorp Metway noted that the FSR legislative package allowed for a two-year transition period 'stated well in advance of the final package reaching Parliament'. It argued that implementation of the FSR should serve as a useful precedent for implementation of the AML/CTF regime.[28]

3.33 The Treasury also supported sufficient lead time for implementation of the AML/CTF regime requirements:

> This is particularly necessary where the measures necessitate substantial changes to information systems and processes, and require training for staff so that they can discharge their obligations under the legislative regime. In supporting this approach we are mindful of the experience in implementing the FSR Act which demonstrated that industry requires a sufficient implementation period to allow it time to understand its new obligations and their implications at a practical level. In addition, industry will often call for guidance as to how it can meet its new obligations and in this regard it is important for policy advisers to remain engaged to ensure that implementation of the measures proceeds in a way that is consistent with the policy intention.[29]

3.34 The Australian Friendly Societies Association submitted that the new regime will require significant changes to systems and processes which cannot be underestimated:

> The AML/CTF package will involve major changes to systems and procedures, potentially requiring new systems, as well as workforce training requirements, which will create significant demands and resourcing issues from both a costs and personnel perspective. Therefore, serious consideration must be given to ensuring that a transition period of as long as possible a duration is provided – we would be suggesting at minimum a 2 year transition period from the date of Royal Assent of the AML/CTF package.[30]

3.35 The ABA pointed out that, since the Exposure Bill extends to a range of financial service providers not currently covered by the FTR Act, the level of change required for these entities will be particularly significant: 'culturally, technologically and procedurally'.[31]

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27 *Submission 2*, p. 3.

28 *Submission 14*, p. 5.

29 *Submission 29*, p. 2.

30 *Submission 17*, p. 2.

31 *Submission 18*, p. 25.

Purported risk-based approach

3.36 The majority of industry bodies who made submissions to the committee's inquiry argued that, despite the purported risk-based approach, the Exposure Bill is overly prescriptive, expansive and unbalanced. Many noted that there are areas of the Exposure Bill where prescriptive and mandatory requirements have replaced a risk-based approach, with very little scope left for industry guidelines.[32] This is undesirable since it imposes a disproportionate burden on business and is inconsistent with good regulatory practice.[33]

3.37 They argued that, further, since the regime captures a wide range of reporting entities and transactions, a 'one-size-fits-all' framework of prescriptive obligations is undesirable as, arguably, this would have serious flow-on effects on business and the general public in terms of inconvenience and compliance costs. Moreover, it may not provide the optimum means of combating money laundering and terrorist financing in Australia.[34]

3.38 In evidence, Mr Brett Knight from American Express told the committee that initially the Exposure Bill had taken on a risk-based approach and that many of the Rules, as they began to form in some of the consultative working groups, had taken an overarching risk-based approach. However, in his view, the proposed regime has begun to take on a more prescriptive approach as the Exposure Bill and the Rules have undergone development:

> What has happened is that the AUSTRAC working groups have 40 people from 40 different industries putting up examples of how their operations work and this and that. AUSTRAC is trying to take all of this and, instead of creating overarching risk principles, they have started to prescribe in very strict detail what institutions should do. As you can appreciate, a global company like American Express has complied with the USA Patriot Act for years and the last thing we would like to see is legislation come in that is prescriptive and contrary to our requirements in other jurisdictions. It makes us invest millions of dollars where we do not think that is effective.[35]

3.39 Many argued also that the measures in the Exposure Bill go far beyond the FATF Recommendations, further than comparable overseas AML legislation, and beyond the AML and CTF objectives stated by the Federal Government as the rationale for the Exposure Bill.

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32 For example, CPA Australia & The Institute of Chartered Accountants in Australia, *Submission 7*, p. 2; Australian Bankers' Association, *Submission 18*, p. 2.

33 *Submission 18*, p. 7.

34 For example, Australian Privacy Foundation, *Submission 4*, p. 4; CPA Australia & The Institute of Chartered Accountants in Australia, *Submission 7*, p. 2; Ms Catherine Kennedy, The Institute of Chartered Accountants in Australia, *Committee Hansard*, 14 March 2006, p. 43; ING Direct, *Submission 13*, p. 2.

35 *Committee Hansard*, 14 March 2006, p. 51.

3.40 The following section of the committee's report examines these issues in more detail.

FATF Recommendations

3.41 The Introduction to the FATF Recommendations states that:

> … FATF recognises that countries have diverse legal and financial systems and so all cannot take identical measures to achieve the common objective, especially over matters of detail. The Recommendations therefore set minimum standards for action for countries to implement the detail according to their particular circumstances and constitutional frameworks.[36]

3.42 A number of submissions and witnesses argued that the proposed AML/CTF regime, despite being touted as a measure to bring Australia into line with the FATF Recommendations, in fact departs from those recommendations in a number of key respects.

3.43 Liberty Victoria argued that the Exposure Bill extends beyond the FATF Recommendations and the existing regime of the FTR Act 'without apparent justification'.[37] Liberty Victoria pointed to some differences:

> … while the FATF 40 Recommendations and the FTRA focus on financial institutions, the Bill focuses on the provision of certain services. While the FATF 40 Recommendations stipulate a threshold transaction of over A$20,000, the Bill proposes one of A$10,000. The Bill's suspicious reporting requirements go far beyond the FATF 40 Recommendations and even substantially extend the already extensive obligations in the FTRA. The Bill contains novel requirements concerning funds transfers and registration of remittance service providers which are found nowhere in the FATF 40 Recommendations or the FTRA.[38]

3.44 The Australian Privacy Foundation (APF) made a similar argument, noting that:

> The Objects clause (Section 3) focuses almost entirely on the need to meet 'international obligations' in the areas of money-laundering and terrorist financing – specifically the Financial Action Task Force (FATF) Recommendations. Apart from being seriously misleading by omission…this focus is not supported by any rigorous analysis of what is actually required to meet those Recommendations.[39]

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36 FATF Documents on the Forty Recommendations, p. 3 at http://www.fatf-gafi.org/document/28/0,2340,en_32250379_32236930_33658140_1_1_1_1,00.html#40recs (accessed 10 February 2006)

37 *Submission 26*, p. 2.

38 *Submission 26*, p. 2.

39 *Submission 4*, p. 4.

3.45 The APF also submitted that international comparisons show that 'there is considerable flexibility for signatories to interpret the Recommendations, and not all jurisdictions are putting in place such a comprehensive identification, reporting and monitoring regime'.[40] Therefore, in the APF's view:

> … the Australian Government is being highly selective in using the FATF Recommendations to support its wider policy objectives where it suits, and at the same time being deliberately vague about those aspects of the existing FTR Act, and draft Bill, which go beyond the FATF requirements.[41]

3.46 Mr Tony Burke from the ABA emphasised the point that the FATF recommendations recognise a risk-based approach which is not reflected in the proposed regime:

> As recognised in the FATF recommendations concerning the measures to be taken by financial institutions and agreed by government and industry, the entire approach should reflect a risk based approach in order to ensure that appropriate resources are matched to high-risk activities and functions. The proposed regime is not risk based either at global or structural level, nor in relation to specific obligations. Generally a risk based approach should match the obligations imposed on an entity with the risks faced by that entity in a proportional and balanced way. More demanding obligations should be imposed to manage more serious risks.[42]

3.47 Mr Burke told the committee that the proposed regime's approach 'is inconsistent with what w[as] agreed with the minister and the Department last year at the roundtable meetings, inconsistent with FATF recommendations, and inconsistent with best practice internationally.[43]

Elements of a true risk-based approach

3.48 Many submissions and witnesses to the committee's inquiry maintained that the industry preference is not for prescription but rather for guidance and information from AUSTRAC about AML/CTF risks, and AUSTRAC's expectations about industry's response to those risks. Essentially, they argued that the obligations of reporting entities should be commensurate with self-assessed risk.

3.49 As The Association of Superannuation Funds of Australia (ASFA) submitted:

> A genuinely risk-based approach should set down high-level principles in line with the FATF requirements. Reporting entities would then be able to introduce their own policies and procedures that are appropriate given the

40 *Submission 4*, p. 4.

41 *Submission 4*, p. 4.

42 *Committee Hansard*, 14 March 2006, p. 2.

43 *Committee Hansard*, 14 March 2006, p. 2.

> risks presented by their products and customers as well as the entity's size and capacity.[44]

3.50 The FPA argued that one of the main benefits of principles-based legislation is that it is capable of being applied confidently by businesses in a flexible way to suit their particular needs and clients:

> By being overly prescriptive, whether in standards or legislation, businesses irrespective of size, structure or business model, are unable to determine appropriate ways of incorporating the requirements into their businesses. It should be possible to innovate within the broad bounds of Government policy without having to seek explicit approval from the regulator.[45]

3.51 Mr Tony Burke from the ABA also provided the committee with an industry view of the requirements of a true risk-based approach:

- first, legal obligations should be framed so that the scope of the legal obligations are clear and the entity subject to the obligations is be able to determine what needs to be done to comply;
- second, compliance with the legal obligations should be feasible and practical and the entity subject to the legal obligations should be able to do what is needed to comply; and
- third, appropriate enforcement mechanisms should be in place whereby the entity subject to legal obligation is subject to reasonable and proportionate sanctions in cases of non-compliance.[46]

3.52 With respect to appropriate enforcement mechanisms, Mr Burke submitted that these are most effectively achieved by an overriding object in the interpretation part of the relevant legislation that makes clear that, both qualitatively and quantitatively, each obligation is to be interpreted consistently with a risk-based approach relevant, for example, to the nature, scale, complexity and risk profile of a reporting entity's business. As part of this overriding part, a global defence for reasonable steps and due diligence should be included.[47]

3.53 Insurance Australia Group (IAG) emphasised that a risk-based approach should start from the assumption that most customers are not money launderers, and that businesses should be able to identify where financial crime risks lie in their own business:

> This approach allows firms to focus their efforts where they are most needed and where they will have the most impact. Factors to be considered can include issues such as jurisdiction, customer type, class of business and

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44 *Submission 28*, p. 2.

45 *Submission 24*, p. 3.

46 *Committee Hansard*, 14 March 2006, p. 2.

47 *Committee Hansard*, 14 March 2006, p. 2.

> distribution channel. Taking a proportionate, risk based approach to anti-money laundering can have significant benefits to businesses, being cost effective (identifying where limited resources need to be deployed) enabling firms to identify and focus on high risk areas.[48]

3.54 Mr Luke Lawler from the Credit Union Industry Association (CUIA) also stressed the need for any AML/CTF measures to be reasonable and proportionate, particularly in the context of community expectations and community understanding:

> … everyone opposes money laundering and everyone opposes terrorism financing. There is no argument there. It is a question of what is realistic and proportionate and what are reasonable expectations in the community about information—what is suspicious; what is unusual; and what people consider to be a reasonable approach to tackling these money-laundering problems and terrorism financing problems. The point I am making is: potentially, it could be quite a monster. It depends on everyone taking a reasonable approach and, to some extent, the very first audit that AUSTRAC does of an institution will determine the shape of the regime.[49]

3.55 In their joint submission, CPA Australia and The Institute of Chartered of Accountants in Australia argued that the proposed regime 'is not adequately factoring in commercial realities and the practicalities of undertaking business in Australia' since, in their view, it will 'deliver complex, over-burdensome regulation'.[50] Further:

> It is a concern that despite the government's stated commitment to improving the regulatory process, there is an ongoing failure of agencies to reconcile their regulatory objectives with the commercial environment. A more focused risk based approach will result in a more robust partnership between industry and government to better monitor money-laundering and terrorism financing.[51]

3.56 The FPA again drew comparisons with the FSR regime which, while also purporting to be principles-based, has in its view been too prescriptive in nature. In relation to the AML/CTF regime, the FPA submitted that in order for it to be truly principles-based, 'it should explicitly recognise the role of risk in determining the extent of obligations'.[52] Further:

> Due to the shortcomings of the Exposure Draft in recognising the role of risk, it is only natural that industry has sought to see the whole of the draft regime – the Exposure Draft and subsidiary draft rules and guidelines –

48 *Submission 11A*, p. 7.

49 *Committee Hansard*, 14 March 2006, p. 9.

50 *Submission 7*, p. 1.

51 *Submission 7*, p. 2.

52 *Submission 24*, p. 3.

> before committing themselves to definitive comments on the proposed legislative package.[53]

3.57 Mr Mark Mullington from ING Direct emphasised the need for the regime to focus on *outcomes*, as opposed to compliance:

> We believe that, with legislation that is too prescriptive and coupled with relatively severe civil and criminal penalties or sanctions, we run the risk of the whole emphasis of the industry being on compliance. In other words, it will become a tick-the-box exercise. That is a little bit similar to where we have ended up with FSRA. It is fundamentally about compliance; it is fundamentally about ticking the boxes.
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> The alternative is a risk based approach which really pushes institutions down the track of outcomes, in that an institution needs to build an anti-money laundering and CTF program to achieve certain outcomes. The regulator has the ability to review those programs and opine on whether they are adequate to achieve those outcomes or not, but it does not push the organisation down the track of compliance. We believe that the way the rules—the three that we have got—have developed to date are quite explicit, quite prescriptive and not risk based.

3.58 The Treasury also expressed its support for a risk-based approach:

> The financial sector comprises a broad range of institutions and service providers offering a diverse suite of products with varying features and risk profiles. The application of the AML/CTF obligations should take that diversity into account and ensure that the intensity of obligations is commensurate with the risks posed by particular products, the profile of the customer and the delivery method of the financial service.[54]

Comparable overseas legislation

3.59 The committee received some evidence pointing to the AML/CTF experiences in the United Kingdom (UK) and the United States (US), and the lessons that Australia might learn from those experiences.

3.60 For example, the ABA submitted that:

> The United Kingdom (UK) and the United States of America (USA) have had considerable experience with the implementation of AML/CTF regimes and have led international efforts in this area. Both countries have sought to implement regimes that are risk-based, consistent with international requirements, best practice and their domestic legal environment. Further, both countries have had significant enforcement experience.[55]

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53 *Submission 24*, p. 3.

54 *Submission 29*, p. 3.

55 *Submission 18*, p. 7.

3.61 However, Mr Tony Burke from the ABA informed the committee that the UK experience was not without its problems as the UK 'initially went down a much more strongly prescriptive path than is currently the case and found enormous difficulty in doing so'.[56] In particular, Mr Burke noted that:

> There is head legislation; then the body of the detail was in guidance notes produced by … the Joint Money Laundering Steering Group. There were significant obligations, for example, in the verification of existing customers, not risk based. They found great difficulty implementing those obligations and significant customer push-back, and they have withdrawn from that approach to a more risk based approach. The UK is probably the model which we point to. There was a bad experience in doing it that way but now the new approach seems to be working far more effectively.[57]

3.62 IFSA also highlighted the UK experience as one which Australia could learn from, noting that it 'would be a costly and wasteful exercise that neither the industry nor the Regulator…would want to go through'[58] if Australia were to get its regime wrong in the first place.

3.63 Mr Brett Knight from American Express emphasised the importance of Australia utilising the experiences of other jurisdictions:

> There is a lot of international experience. The US implemented this type of legislation four or five years ago, and so has the UK. In my opinion and from what I have seen, the regulators have not really taken a lot of this global experience and applied it. In the AML-CTF advisory group meetings last week, there was a whole discussion on creating risk matrixes, which have been compiled very comprehensively in other jurisdictions for years. So I think they have not used the opportunity to look at other global jurisdictions that have this type of legislation to get best practices effectively.[59]

3.64 SunCorp Metway suggested that 'the final version of the Exposure Draft be rigorously compared' by the Department and/or AUSTRAC 'to assess parity with existing UK and US AML legislative models' to ensure that Australian requirements do not exceed those in other similar jurisdictions.[60]

Department response

3.65 In response to industry concerns with respect to the overly prescriptive approach taken in the Exposure Bill, a representative from the Department maintained that the Exposure Bill is principles-based with a risk base beneath it. The

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56 *Committee Hansard*, 14 March 2006, p. 10.

57 *Committee Hansard*, 14 March 2006, p. 10.

58 *Submission 2*, p. 4.

59 *Committee Hansard*, 14 March 2006, p. 51.

60 *Submission 14*, p. 4.

representative stated that there is no explicit definition of 'risk-based' but that 'the concept is clear'. That is:

> The principles are in the legislation and then there is flexibility for the industry to determine, using a risk based assessment, what their regime shall be. Then that will be embodied in an AML-CTF program, which will be subject to audit.[61]

3.66 The representative also pointed out that the concerns of industry in relation to this issue have 'been taken on board' and that 'the documents that finally emerge from this process – the vital rules that need to be drafted – will reflect that discussion'.[62]

3.67 A representative from AUSTRAC confirmed that, specifically in relation to the AML/CTF Program Rules, 'we are feeling fairly comfortable that we have achieved a risk based approach – a set of rules that set out a framework in which entities can judge their own risk and deal with that in an appropriate way'.[63] She also noted that the Customer Identification Rules would be progressing on a similar basis.[64]

3.68 With respect to reference by some submissions and witnesses to the situation in the UK, a representative from the Department told the committee that 'some of the suggestions about learning from the UK experience might in fact be extrapolating from that, as opposed to considering whether [for example] the detail in their identification requirements is actually less or more than our suggestion'.[65]

3.69 Another departmental representative explained that it should be recognised that there are differences between the UK and US experiences on the one hand, and the Australian situation on the other:

> Yes, we have heard it said that we should be learning from the overseas experience. We accept that entirely and we have looked at the overseas experience, especially the UK and the US. But there are differences with the Australian system. I do not think we can pick up and apply overseas provisions slavishly. We have to modify them for the Australian environment. I make the point that although we can look at the UK experience there are limits to how far we can take that.[66]

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61 *Committee Hansard*, 14 March 2006, p. 67.

62 *Committee Hansard*, 14 March 2006, p. 68.

63 *Committee Hansard*, 14 March 2006, p. 68.

64 *Committee Hansard*, 14 March 2006, p. 68.

65 *Committee Hansard*, 14 March 2006, p. 63.

66 *Committee Hansard*, 14 March 2006, p. 63.

Practical impact of the proposed regime

3.70 The committee received evidence from a variety of financial services industry sectors indicating that there are a number of common residual concerns regarding the practical impact of specific aspects of the proposed AML/CTF regime. The major concerns raised with the committee will be considered below.

Scope and coverage of the Exposure Bill – 'designated services'

3.71 Some submissions and witnesses commented on the wide scope of the Exposure Bill. For example, CPA Australia and The Institute of Chartered Accountants in Australia argued that, despite the Federal Government's claim that the first tranche of reforms will only impact on the financial services sector and businesses in competition with that sector, 'the definitions of designated services are so broad that they currently cover all businesses which provide trade credit' so that:

> … all consumer credit transactions will … be caught, so individuals buying a new television or fridge on credit will now be subject to full Customer identification procedures and will have to produce a birth certificate and/or other primary and secondary documents.[67]

3.72 In this respect, '(t)he descriptions of certain designated services in clause 6 of the Bill go far beyond the FATF Recommendations'.[68]

3.73 IAG agreed that the Exposure Bill's definition of 'business' is unqualified and, therefore, inconsistent with the FATF Recommendations. In IAG's view, the FATF Recommendations are:

> … expressed to impose obligations on 'financial institutions' (and in certain circumstances on 'non-financial businesses and professions'). 'Financial institution' under the FATF recommendations is defined as 'any person or entity who conducts as a business one or more' of the prescribed activities. The Draft Exposure Bill ignores this important qualification.[69]

3.74 IAG also made the point that the definition of 'business' in the Exposure Bill, by extending to one-off and occasional activity, goes beyond the FATF Recommendations. It argued that 'there is some scope for the ambit of the definition of "business" to be reduced without making it inconsistent with the FATF Recommendations'.[70]

3.75 The ABA noted that the list of designated services does not draw any distinctions on the basis of monetary limits (except a $1000 limit for stored value cards); nor does it take into account whether activity is carried out on an occasional or

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67 *Submission 7*, p. 2.

68 *Submission 7*, p. 2.

69 *Submission 11A*, p. 6.

70 *Submission 11A*, p. 6.

a regular basis; nor does it recognise to whom the service is provided (for example, a related company).[71]

3.76 In relation to the threshold issue, Ms Michelle Mancy from American Express argued that to support a risk-based approach, 'meaningful thresholds should be set' since 'there is no appreciable risk of money laundering below certain minimal levels of transactional activity' and '(t)he absence of thresholds means it is simply overburdensome to require this kind of identification'.[72]

3.77 Ms Mancy elaborated:

> There are no thresholds for any designated service except stored value cards and we would like to see a threshold for consumer credit arrangements. American Express card members spend more than customers of other institutions. Even so, the average spend on the American Express card in Australia is not more than $10,000 each year.
>
> The reporting threshold should be increased as the current $10,000 figure dates back to the early days of the FTRA over 10 years ago and is no longer reasonable. It should be adjusted to account for inflation. The current $10,000 figure is also set substantially below the FATF recommendations. Lowering the threshold leads to significant increased compliance costs and there is no evidence that Australia presents higher risks than other countries with similar income levels.[73]

3.78 Others agreed that the threshold should be increased. The Deputy Privacy Commissioner told the committee that:

> Our view is that the Financial Transaction Reports Act has been in place for quite some years now, and the original threshold was set back in the early nineties. It may be useful to have that reviewed to see whether it is still an appropriate amount, so the basis of our comment there is generally on the length of time for which that amount has been set.[74]

3.79 Ms Johnston from the APF submitted that a threshold of approximately $US15,000 might be more appropriate:

> We believe there should be a threshold for all three categories: international transactions, domestic transactions and suspicious transactions—if you keep the third category. As Mr Pilgrim has mentioned, we believe the $10,000 threshold that was set some time ago is now too low, through the effects of inflation. If you want to pull a figure out of a hat, I would say

71 *Submission 18*, p. 9.

72 *Committee Hansard*, 14 March 2006, p. 48.

73 *Committee Hansard*, 14 March 2006, p. 48.

74 *Committee Hansard*, 14 March 2006, p. 33.

> something like $US15,000—so whatever that is in Australian dollars; it might be $A18,000 or $A20,000—might be more appropriate.[75]

Department response

3.80 In response to suggestions that the transaction threshold of $10,000 should be reviewed, a representative from AUSTRAC informed the committee that there are currently no plans to do so:

> Certainly we do not believe that there is any reason to review that level at the moment. Reporting at that level is of use to AUSTRAC and its partner agencies in their work. People from the privacy groups in particular have raised this in AUSTRAC's privacy consultative committee. While we are always open to reviewing that if necessary, at this stage we believe that the $10,000 threshold is still a reasonable threshold to have.[76]

3.81 In an answer to a question on notice, AUSTRAC expressed its view that $10,000 remains the appropriate level for the threshold:

> While the number of transactions at this level has increased, this amount remains significant. The Bill does provide for the threshold to be raised, as well as lowered, by regulation, not by AUSTRAC. The amount will be kept under continuing review and if it appears that it should be raised, recommendations will be made to the Minister for Justice and Customs about the need for regulations.[77]

Identification procedures (Part 2)

3.82 Most of the detail in relation to customer identification requirements will be contained in (as yet unreleased) Rules. This has created uncertainty for a number of groups who participated in the committee's inquiry.

Not risk-based and overly complicated

3.83 Some submissions and evidence argued that the customer identification requirements in Part 2 of the Exposure Bill are not risk-based. For example, Mr Tony Burke from the ABA told the committee that:

> … there is a failure to distinguish between high- and low-risk products through the definitions, which results in obligations that are not proportionate to risk. Rules relating to 'know your customer' are too complex and excessive for low-risk services. Key aspects of the operation of this part are contained in the rules. Without knowing the content of the rules, it is not possible to determine whether the scope of the obligation is

75 *Committee Hansard*, 14 March 2006, p. 33.

76 *Committee Hansard*, 14 March 2006, p. 69.

77 *Submission 33*, p. 3.

> sufficiently clear and whether regulated institutions will be capable of complying.[78]

3.84 CPA Australia and The Institute of Chartered Accountants in Australia agreed, particularly in relation to the customer due diligence requirements in Part 2:

> The requirements to perform Customer Due Diligence set out in Part 2 of the Bill are not risk based. They only provide for the exemption of certain services which must be specified in the AML/CTF Rules. The requirements of Part 2 and the AML/CTF Rules on Applicable Customer Identification Procedures apply to all other designated services, regardless of the level of risk posed by the customer, type of service or method of delivery or the jurisdictions in question (eg where the customer resides or where the product or service is to be delivered). This is an unnecessarily inflexible framework for the identification of customers.[79]

3.85 CPA Australia and The Institute of Chartered Accountants in Australia argued further that, despite proposed section 35 allowing for the exemption of designated services which are considered to be low risk:

> There is no consideration to be given to the risks associated with the customer or any other aspect of the transaction. In general terms, the designated service of processing transactions through an accountant's trust account may have some potential for risk and may not generally meet the AUSTRAC criteria as a low risk service for exemption. However, the customer, source and destination of the trust account transaction may all be of a low risk in relation to money laundering and/or terrorist financing. Despite this, they are unlikely to be services excluded from the application of Part 2 of the Bill or to which a lower level of Customer Due Diligence is applicable.[80]

3.86 Platinum Asset Management (Platinum), an Australia domiciled investment manager specialising in international equities, queried the burdensome nature of the obligations in Part 2:

> Given that all investment money comes to Platinum via the Australian banking system (which is subject to rigorous regulation) what benefit will be gained from requiring us to further scrutinise the identity of our clients?[81]

3.87 The ABA argued that the requirements in the draft Rules relating to 'Know Your Customer' and customer due diligence are too complicated:

> Industry proposed, in November 2005, that customer due diligence and enhanced customer due diligence be simplified into a unified approach but

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78 *Committee Hansard*, 14 March 2006, p. 3.

79 *Submission 7*, p. 5.

80 *Submission 7*, p. 5.

81 *Submission 21*, p. 3.

> this has not appeared in the E[xposure] D[raft Bill]. The lack of further release of the suite of identification rules is making it almost impossible for industry to assess the scope of these due diligence requirements and their impact on businesses (and their customers).[82]

3.88 The ABA also highlighted the intrusiveness of the identification requirements for clients and customers:

> The proposed Customer Due Diligence will require customers to spend longer conducting transactions and a significant proportion may feel the information required under the proposed regime is invasive, particularly in relation to provision of information on country of birth, residence and citizenship. International experience indicates that this information is of little value in AML/CTF control and there is concern that an obligation to ask for a place of birth may raise complaints of 'racial profiling' from many customers.[83]

Electronic verification

3.89 A number of submissions and witnesses raised concerns that, while the Exposure Bill and the Rules are technologically neutral, electronic verification (EV) processes with respect to customer identification have not been expressly provided for. These groups argued that express recognition of EV should be set out in the Rules and should encompass current EV methods used by industry.[84] The committee understands that many businesses currently use EV to check customer information by carrying out (or engaging third party commercial service providers to carry out) searches of electronic databases that store information about people.

3.90 IFSA noted that this issue is critical to the financial services sector because it predominantly interacts with existing customers and potential customers on a non face-to-face basis.[85] By way of example of the significance of the EV process, Ms Lisa Claes from ING Direct informed the committee that eighty per cent of that company's new customers are verified using EV. American Express argued that EV 'is equally if not more robust than human inspection of documents … which may be forged or manipulated' and is, in fact, 'a powerful tool to thwart illicit activity'.[86]

3.91 American Express asserted that it is imperative that the proposed regime 'does not prescribe a narrow, traditional identification process based on physical or face-to-

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82 *Submission 18*, p. 14.

83 *Submission 18*, p. 14.

84 For example, American Express Australia Limited, *Submission 15*, pp 2-3; GE Capital Finance Australasia Pty Ltd, *Submission 22*, p. 1; PayPal Australia Pty Ltd, *Submission 16*, pp 1-2; Securities & Derivatives Industry Association, *Submission 31*, p. 3; Ms Lisa Claes, ING Direct, *Committee Hansard*, 14 March 2006, p. 50.

85 *Submission 2*, p. 6.

86 *Submission 15A*, pp 2 & 3.

face presentation or inspection of identity documents, especially as more efficient alternatives are available'.[87] In this context, the concept of competitive neutrality is particularly relevant, since businesses such as American Express do not have physical branch networks through which to conduct face-to-face inquiries with clients:

> If the law does not allow ample flexibility and adaptability for financial institutions to adopt customer identification methodologies that are feasible within their business models, the legislation may have extremely negative impacts on competitiveness, business growth and expansion, without assisting the task of identifying and preventing unlawful activity. This will create unnecessary burden on financial institutions and businesses that operate in a non face-to-face environment and will curb business growth and expansion into non traditional channels – such as internet banking, global payments solutions and many other products & services that are provided in a non face-to-face environment.[88]

3.92 The ABA noted that the Department recently made it clear at a recent working group meeting that 'the intention (not reflected in the drafting) was to permit reporting entities to decide whether to adopt the face-to-face procedures or the non-face-to-face procedures, based on which is best suited to their business processes'.[89]

3.93 At the committee's hearing a representative from the Department explained that EV has not been expressly included in the Rules for the following reasons:

> It will not necessarily be expressly provided for because, under a risk based system, you do not have to express things because that would become prescriptive but certainly the intention is there. This is the problem that you run into. People want risk based flexibility. At the same time they want clear guidance on what they are required to do. I think that is fair enough, because different industry sectors want different things and we have to have a process which allows each of them to be given what they need.[90]

3.94 The representative continued:

> The message has been heard loud and clear. The minister in roundtable conferences has basically said that there has to be an electronic verification system ... The idea of this is not to stop legitimate industry which is operating in a certain way from operating in that way, unless the risks of money laundering are so high that they should not be operating in that way. You cannot take an industry which operates entirely in an electronic environment and say, 'Next week you have to have branches because of these provisions.' That has been the challenge: to come up with electronic

87 *Submission 15*, p. 3.

88 *Submission 15A*, p. 1.

89 *Submission 18*, p. 15.

90 *Committee Hansard*, 14 March 2006, p. 73.

> verification procedures which are as robust as paper—leaving aside, for the moment, how robust paper identification and verification are.[91]

3.95 Further:

> The risk based approach will say that you as an entity have to have robust verification procedures and if you are satisfied that electronic verification is sufficiently robust and is appropriate then an entity can develop that. That is a risk based approach. Then, the onus will move on to our good friends at AUSTRAC with their audit function. We think that the Attorney-General's Department is likely to be involved in further debate and discussion about what the electronic verification involves. I do not think that issue is going to go to bed for quite some time but we are talking about an implementation period for this legislation; we are not talking about everything being in place on day one.[92]

Third party verification

3.96 Some argued that the procedures relating to third party verification of customer identification may not be practicable.

3.97 For example, Mr Mark Mullington from ING Direct noted that ING Direct is one of the largest providers of home loans through the mortgage broker channel. He acknowledged that the proposed regime contemplates third parties such as mortgage brokers undertaking the identification process on behalf of lending institutions, however he pointed out that 'the exact mechanism for this at this stage is unclear'.[93] Further:

> … the way the draft bill operates, it will create complexity and bureaucratic burden for the mortgage broker channel. It also creates serious concerns regarding our reliance on mortgage brokers undertaking that identification. We believe the legislation needs to contemplate an accreditation and registration process—that is, individuals and organisations become accredited to undertake the customer identification and verification process and, subject to certain controls, financial institutions be permitted to rely in good faith on that identification. At this stage, we are continuing to work with AUSTRAC on developing a viable solution.[94]

3.98 CPA and The Institute of Chartered Accountants in Australia argued that the third party verification requirements are not workable in relation to the services provided by accountants and would lead to unnecessary duplication of resources of both accountants and customers:

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91 *Committee Hansard*, 14 March 2006, p. 73.

92 *Committee Hansard*, 14 March 2006, p. 73.

93 *Committee Hansard*, 14 March 2006, p. 49.

94 *Committee Hansard*, 14 March 2006, pp 49-50.

> Clause 34 of the Bill allows a reporting entity to authorize another person in writing to conduct the applicable customer identification procedures required in Part 2. This presumes that the services are being provided concurrently. However, an accountant who is a reporting entity will be providing services to a client who is likely to have previously had services provided by another reporting entity which has already conducted customer identification procedures. The Bill does not allow the accountant to rely on that previously conducted customer identification. Coming at the end of the 'chain' of reporting entities the accountant cannot provide written authorization for another reporting entity to carry out the applicable customer identification procedures.[95]

3.99 Mr John Anning from the FPA also raised third party identification as a issue for financial planners:

> Third party identification is a key issue, because often financial planners are seen as the first link in a chain of financial services transactions. So it is vital for us to understand how financial planners will be impacted by the regime, and to do that we need the draft rules and guidelines for third party identification. It raises practical issues. A financial planner may be undertaking identification on behalf of a number of financial institutions, and if they each have their individual risk assessment processes they may rate products and customers at different risk levels—therefore requiring identification to be done at various levels. So this has the outcome that the financial planner conducts an initial identification of the client, covering the maximum information required, just to cover all possibilities.[96]

3.100 The Securities & Derivatives Industry Association (SDIA) argued that certain arrangements involving third parties should be exempt from the due diligence requirements:

> Where an AFSL licence holder is a reporting entity and proposes an arrangement with another AFS licensee such an arrangement should be exempt from the due diligence requirements. These entities have already been through an in depth screening process in their licence applications and, if there is no adverse finding against them by the Australian Securities & Investments Commission (ASIC) after the receipt of the licence, the reporting entity must be able to do business with them in the normal course. The expectation should be that they also comply with AML/CTF legislation and that they have completed the customer identification process for their clients. Both licensees should not be required to obtain customer identification – only the primary contact. Similarly, it should not be a requirement that reliance on another licensee requires that a stockbroker review and approve the process for customer identification employed by that other licensee. Examples of these types of arrangements are

95 *Submission 7*, p. 5.

96 *Committee Hansard*, 14 March 2006, p. 17.

> stockbrokers having arrangements with financial planners and other intermediaries, margin lenders and managed fund providers.[97]

3.101 Allens Arthur Robinson (Allens) pointed out that, while proposed section 34 authorises third parties to carry out customer identification procedures, proposed section 12 prohibits them from providing information obtained by that procedure to anyone other than the reporting entity. Allens argued that:

> In order to facilitate the sharing of information between related entities in a group structure (and thereby reducing costs) … external agents should be able to provide customer identification information to related entities of the reporting entity if so authorised by the reporting entity.[98]

Technical issues

3.102 Allens also drew the committee's attention to the interaction between the customer identification procedures required by the Exposure Bill and the 'Know Your Customer' and risk classification requirements of the AML/CTF Program Rules. Mr Peter Jones from Allens summarised the crux of the issue as follows:

> … the exposure draft appears not to require reporting entities to take any action in relation to what we would call dormant customers—people who, at the time of commencement of the act, as it would be then, would not be having designated services provided to them. But when we look to the rules that have been released, the one that deals with AML compliance programs, for example, seems to suggest that all customers need to be risk classified and that reporting entities need to consider whether they need to get further K[now] Y[our] C[ustomer] information in relation to all customers and whether they need to update the KYC information they do hold in respect of all customers. To us, that gives rise to the question of whether that is the intention and, if it is, whether AUSTRAC does actually have the power to make rules which do not appear to have any legislative basis.[99]

3.103 Allens' submission noted that this is relevant for two reasons:

> In the first instance the extension of the AML/CTF program rules to customers who may no longer have an ongoing relationship with the reporting entity and no KYC obligations under the Act has practical and resource implications.
>
> More importantly if the Rules can regulate beyond the Act it is imperative that AUSTRAC's Rule making power is subject to, (at the least) industry consultation and some form of parliamentary scrutiny. At present it is not.[100]

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97 *Submission 31*, pp 3-4.

98 *Submission 27*, p. 4.

99 *Committee Hansard*, 14 March 2006, p. 56.

100 *Submission 27*, p. 3.

3.104 In evidence, Mr Jones submitted that the proposed regime's inclusion of both past and present customer identification, poses the following questions:

> … how far back do you go? Where do you draw the line? That is the practical issue. Who is a dormant customer? Who is beyond the reach of needing to be risk classified? If they have not done anything with you for five years and then walk in the door tomorrow, are they a new or an existing customer? Part of this will be dealt with when we get the rules about continuity of relationships and what disqualifies a relationship from being a continuous one. I do not want to jump the gun on that score, but I do think you need to address the practical issue about dormancy.[101]

3.105 In response to a question on notice from the committee in relation to some of the technical issues raised by Allens, the Department advised that:

> The Attorney-General's Department is currently considering a range of issues raised in submissions to the Senate Legal and Constitutional Committee's Inquiry. The submission from Allens Arthur Robinson raises seven sets of issues, all of which will be addressed as part of the Department's consideration of suggested amendments to the exposure draft AML/CTF Bill.[102]

3.106 With specific reference to concerns about AUSTRAC's rule-making power, a representative from the Department indicated that consultation by AUSTRAC with industry and law enforcement groups when making the Rules might also be properly supplemented by consultation with privacy groups.[103]

Reporting obligations (Part 3)

3.107 Some submissions and witnesses commented on the reporting of suspicious matters requirements in Part 3 of the Exposure Bill.

3.108 For example, Mr Tony Burke from the ABA told the committee that:

> The industry has concerns that the suspicious matter reporting rules may be too prescriptive, as it appears that as many as 24 matters—many of which are difficult to assess—must be taken into account in determining whether there are reasonable grounds for forming a suspicion that would require a suspicious matter report, and as many as 19 details must be included in such a report.[104]

3.109 Mr Peter Jones of Allens pointed out that there is an apparent inconsistency between the scope of the obligation contained in proposed subsection 39(1) of the Exposure Bill and the reporting obligation in proposed subsection 39(2):

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101 *Committee Hansard*, 14 March 2006, p. 58.

102 *Submission 32*, p. 1.

103 *Committee Hansard*, 14 March 2006, p. 74.

104 *Committee Hansard*, 14 March 2006, p. 3.

> That is an issue that we see in the FTRA as well but, given the detailed process—the exhaustive process—we are going through now and the extension of the suspicious reporting regime beyond financial institutions or cash dealers to a much wider audience, we thought it was worth raising this particular point. That point is the apparent mismatch between an objective test as to when one has reasonable grounds to have a suspicion, which might give rise, you would think, to an obligation to report, and the actual obligation to report, which only arises once a suspicion has arisen. It is a technical drafting issue but it is one that we thought was important, given that context.[105]

3.110 Liberty Victoria argued that proposed section 39 goes well beyond the requirements of the FATF Recommendations and also represents a significant extension of the current suspicious reporting regime under section 16 of the FTR Act:

> To portray cl 39 as an implementation of the FATF 40 Recommendations is nonsense. To portray it as a modification of the existing regime to conform with the FATF 40 Recommendations is equally untrue. It is, in truth, a wholesale revision of the suspicious reporting regime, which bears little or no resemblance to the FATF 40 Recommendations and extends the regime well beyond the current law. The Government should be asked to explain why this is necessary.[106]

3.111 Similarly, Allens asserted that elements of proposed section 40 are unworkable in practice and extend beyond the requirements of relevant FATF Recommendations.[107] Both Allens and Liberty Victoria pointed out that proposed section 40's extension of the suspicious reporting obligation to cases where it is suspected that there has been a breach of foreign law is onerous and unrealistic.[108]

3.112 Platinum again emphasised the overly burdensome obligations in the Exposure Bill, the costs of which would ultimately be borne by its small client base:

> Given that all monetary transactions with our clients are executed through an Australian bank, building society or credit union, what benefit will be gained from requiring us (a non-cash intermediary) to replicate the reporting of threshold transactions and international funds transfer instructions that will be carried out (and also reported) by the bank, building society or credit union concerned?[109]

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105 *Committee Hansard*, 14 March 2006, p. 56.

106 *Submission 26*, pp 9-10.

107 *Submission 27*, pp 5-6; Mr Peter Jones, Allens Arthur Robinson, *Committee Hansard*, 14 March 2006, pp 57-58.

108 *Submission 26*, p. 11; *Submission* 27, pp 5-6; Mr Peter Jones, Allens Arthur Robinson, *Committee Hansard*, 14 March 2006, pp 57-58.

109 *Submission 21*, p. 4.

Department response

3.113 In response to some of the issues raised in relation to reporting of suspicious matters, including concerns that reporting entities would be required to consider and have knowledge of offences in foreign jurisdictions, a representative of the committee informed the committee that:

> The intention of those provisions of the legislation is not to require people to become experts in foreign law, Australian law or anything else. What they are intended to do is to ensure that, if people have suspicions about the source of the money or the activities that people are engaged in when they present to them, they then put in a report. I would submit it is a fairly simple concept: if you do not have a suspicion because there is no basis for you having grounds for suspicion then there is no suspicion and there is no report.[110]

3.114 However, despite this contention, the representative expressly acknowledged the comments made by submissions and witnesses to the committee's inquiry in relation to suspicious matters reporting, and indicated that this is an area of the Exposure Bill that would be revisited by the Department.[111]

AML/CTF Programs (Part 7)

3.115 Some specific issues relating to AML/CTF Programs under Part 7 of the Exposure Bill arose in the course of the committee's inquiry, namely:

- the costs involved in implementation of an AML/CTF Program;
- the merging of the separate activities of AML and CTF in AML/CTF Programs; and
- the possible legal implications of a reporting entity rejecting a potential customer on the basis of its AML/CTF Program.

3.116 For example, Mr Luke Lawler from the Credit Union Industry Association highlighted the costs of setting up the AML/CTF Programs:

> There will be a significant cost in setting up the AML CTF program, which is kind of the core of the compliance obligation in this proposed legislation. In the lead-up to the passage of legislation and in the transition period, we will get a better understanding of what the regulators' expectations are about the risks and the response to the risks but it is potentially quite incredibly invasive and intrusive of people's privacy …[112]

3.117 Some argued that money laundering and counter-terrorist financing issues are inappropriately conflated in the Exposure Bill, including the AML/CTF Programs,

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110 *Committee Hansard*, 14 March 2006, p. 62.

111 *Committee Hansard*, 14 March 2006, p. 62.

112 *Committee Hansard*, 14 March 2006, p. 8.

when they are quite distinct activities. As the ABA submitted, '(t)here must be separate and different obligations applying to each threat, with which it is possible in practice to comply'.[113]

3.118 The Australian Friendly Societies Association noted concerns in relation to the possible legal implications of rejecting potential customers on the basis of a reporting entity's AML/CTF Program:

> Concerns have been raised about the legal implications of an organisation rejecting a potential customer on the basis of their AML/CTF program and customer due diligence, particularly where there could be allegations of discrimination on the grounds of race, given the collection of information about country of birth and citizenship. We would query whether consideration has been given to what protections there might be for financial institutions that reject a potential customer and are later subject to legal suit?[114]

3.119 This is particularly significant given that a reporting entity would be unable to reveal to the customer the reasons for rejection (under the 'tipping off' offence in proposed section 95 of the Exposure Bill).[115]

Obligation to 'materially mitigate' risk

3.120 Several witnesses and submissions raised as problematic proposed section 74's requirement that an AML/CTF Program 'materially mitigate' the risk of money laundering and terrorist financing. For instance, Mr Tony Burke from the ABA told the committee that:

> While we have spent quite a deal of time discussing 'materially mitigate' with the department and AUSTRAC, we have not yet come to an agreed position on that. Our concern is that it is too prescriptive. Our concern also is that it will not do the job. An organisation could be said to have materially mitigated risk in that no money laundering had been discovered, so the outcome was positive but the processes were very shoddy indeed. The converse may apply—an organisation may have fantastic processes but, unfortunately, has been the victim of money laundering and hence could be said not to have materially mitigated risk.[116]

3.121 The ABA's submission drew comparisons with the UK and US AML/CTF regimes in relation to this issue:

> Neither of these two countries imposes an obligation to materially mitigate AML/CTF risk as part of the obligation to implement AML/CTF programs.

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113 *Submission 18*, p. 14.

114 *Submission 17*, p. 3.

115 'Tipping off' is discussed more fully later in this report in relation to privacy issues.

116 *Committee Hansard*, 14 March 2006, pp 6-7.

> For example, in the UK, under the Money Laundering Regulations 2003 (ML Regulations), relevant businesses are required to establish internal control and communication procedures which are 'appropriate for forestalling and preventing' money laundering. A defence to prosecution is provided where an entity 'took reasonable steps and exercised all due diligence' to implement such a program. In deciding whether an offence has been committed a court must take into account whether the person followed relevant industry guidance.[117]

3.122 The ABA's submission continued:

> The AUSTRAC response to industry's concerns about "materially mitigate" is that the UK obligation to 'prevent' is a higher standard than mitigation. This response ignores the legislative elements that make the UK approach fundamentally different from the proposed regime. It ignores the qualifier 'appropriate' and critically, ignores the overall defences. The US obligation contains no reference to 'materially mitigate' or to any particular outcome. It requires the establishment of programs (defined solely in accordance with FATF minimum recommendations) with the objective of guarding against money laundering.[118]

3.123 American Express argued that the 'materially mitigate' risk requirement is 'unrealistic and unattainable' since 'it is not possible to quantify levels of money laundering and terrorist activity with any level of precision, nor to predict future directions and developments of such activity'. It suggested that:

> The requirement should be changed to require providers to implement programs which 'effectively mitigate such risks as are reasonably apparent' of the provider's products and services being misused.[119]

3.124 SDIA also argued that clearer guidance is needed on the meaning of 'materially mitigates'.[120]

Secrecy and access (Part 11)

3.125 Some submissions and witnesses raised concerns in relation to Part 11 of the Exposure Bill. Under proposed section 95, reporting entities must not disclose that they have formed an applicable suspicion or have reported information to AUSTRAC under the suspicious matter reporting requirements, or that they have given further information to a law enforcement agency in response to a request.

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117 *Submission 18*, p. 7.

118 *Submission 18*, p. 7.

119 *Submission 15*, p. 4.

120 *Submission 31*, p. 6.

Corporate groups

3.126 Such concerns related primarily to the Exposure Bill's failure to recognise the existence of corporate groups, where customers have multiple products and services, and where the group potentially needs to monitor multiple activities of that class of customers to satisfy the AML/CTF requirements. Conglomerate operations raise a number of complex issues, including the issue of information-sharing between group entities.[121]

3.127 Similarly to the point raised in paragraph 3.101, Allens made the following suggestion in relation to this issue:

> Where the reporting entity is part of a corporate group we suggest that the reporting entity should be able to make the same disclosure to another member of the group, so long as that disclosure is not likely to prejudice an investigation which might be conducted following the report [of a suspicious matter].
>
> As a matter of sound business practice and risk management, if one member of a corporate group has information relevant to an offence or attempted offence it should be able to advise other members of the group of that suspicion, for example, to minimise the likelihood of offences being perpetrated across the group or another member of the group unwittingly facilitating a money laundering or terrorist financing offence.[122]

3.128 American Express also argued that the Exposure Bill should be amended to take reasonable account of corporate group structures and to allow them to share information.[123]

3.129 The SDIA went further, suggesting that:

> … it is important for its members to be able to share information (under notice to AUSTRAC for AML/CTF purposes) regarding certain activities of certain people. This would help prohibit more than one of our members becoming involved with an individual or entity, if the member who first suspected an instance where money laundering or terrorist financing was the reason behind a transaction, could inform other members. To be successful there must be immunity from prosecution for sharing such information. We recognise that tipping off could be a problem arising from such sharing of information as it would be difficult to identify the source however not sharing the information could have a significant impact on the industry.[124]

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121 For example, IFSA, *Submission 2*, p. 7; Suncorp-Metway Limited, *Submission 14*, p. 3; American Express Australia Limited, *Submission 15*, p. 4.

122 *Submission27*, p. 7.

123 *Submission 15*, p. 4.

124 *Submission 31*, p. 8.

Lack of available defences

3.130 The committee also received evidence expressing concern about the lack of defences in the Exposure Bill in relation to the secrecy provisions. Many groups were fearful that legitimate actions by their employees pursuant to obligations under the regime may result in inadvertent breach of proposed section 95.

3.131 Mr Chris Downy of the Australian Casino Association, explained how employees of reporting entities may be caught by the tipping off provisions:

> The concern our members have is this whole question of alerting a high-risk customer to the fact that they are under suspicion. Asking them to provide identification basically alerts them to the fact that they may be under investigation.[125]

3.132 Some suggestions with respect to the tipping off provision included:

- a defence for employees of reporting entities who act in compliance with the Rules and Guidelines;[126] and
- a 'safe haven' provision, where employees of a reporting entity could make a disclosure to a customer as long as that disclosure does not prejudice an investigation.[127]

3.133 A representative of the Department assured the committee that defences to the tipping off offence in the Exposure Bill are available in the Criminal Code:

> We have had this discussion and it has been raised at the outset with industry. There is nothing in here for the moment. What they want is to see a provision in here saying, 'Whatever happens, if you have taken reasonable steps and exercised due diligence, you have a defence against criminal prosecution.' The reason we have not put it in there is because it is odd in these days of having the Criminal Code to have a provision like that in specific legislation. We think it is covered by the Criminal Code.[128]

AUSTRAC resources

3.134 The committee received evidence suggesting that, at the present time, AUSTRAC is not adequately resourced to produce draft Rules in the required timeframe;[129] nor is it resourced to effectively undertake its other obligations under the proposed regime. For example, IFSA suggested that the Federal Government

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125 *Committee Hansard*, 14 March 2006, p. 25.

126 See, for example, Financial Planning Association of Australia, *Committee Hansard*, 14 March 2006, p. 20.

127 See, for example, Mr Peter Jones, Allens Arthur Robinson, *Committee Hansard*, 14 March 2006, p. 57.

128 *Committee Hansard*, 14 March 2006, p. 71.

129 See, for example, IFSA, *Submission 2*, p. 4; ING Direct, *Submission 13*, p. 3.

'consider whether AUSTRAC is adequately resourced to effectively carry out its obligations in relation to its Rule making function'.[130]

3.135 In response to questioning by the committee, a representative from AUSTRAC stated that, in her view, the slow release of the Rules is not a resource issue:

> One of the issues around resources is that having more people will not get the rules out any faster. The rules are so interrelated that the people working on them need to be across all the issues. So we have a group of three particular people who are directly involved in drafting the rules together and who have that across-the-board knowledge to be able to put them together.[131]

3.136 Nevertheless, the committee considers it essential that AUSTRAC be given adequate resources to effectively carry out its obligations under the regime, including its Rule-making function. Such resources should include provision of adequate numbers of staff with appropriate expertise and experience, as well as implementation of strategic planning capabilities within the organisation.

Interaction between the Exposure Bill and other legislative regimes

3.137 Some submissions and witnesses pointed out that the interaction between the Exposure Bill and other legislation must be taken into account when considering the impact of the new regime. Any inconsistencies or overlap must be addressed in order to create certainty for business. For example, Ms Michelle Mancy of American Express argued that:

> The government needs to prioritise laws relating to money-laundering prevention, privacy and discrimination, thereby ensuring that compliance with one will not affect a breach of another, rather than leaving it to business to tip-toe through a minefield of compliance regimes that seem to be at odds with each other.[132]

3.138 The ABA also highlighted the potential inconsistency between the Exposure Bill and other legislation with which financial service providers must comply. It argued that the interrelationship between the Exposure Bill and other laws, including privacy, discrimination, proceeds of crime, corporations and electronic transactions legislation, needs consideration.[133]

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130 *Submission 2*, p. 4.

131 *Committee Hansard*, 14 March 2006, p. 76.

132 *Committee Hansard*, 14 March 2006, p. 49.

133 *Submission 18*, p. 25.

Specific issues arising for particular industry sectors

3.139 The committee also received evidence indicating the existence of specific concerns relating to the following industry sectors:

- superannuation;
- casinos/clubs;
- financial planning; and
- insurance.

3.140 Some of these concerns are discussed below.

Superannuation

3.141 Superannuation fund trustees will be considered reporting entities for the purposes of AML/CTF obligations because they provide a designated service. Evidence provided to the committee highlighted that superannuation raises a number of unique issues. Further, the risk profiles for AML/CTF will differ significantly between the various types of superannuation funds.

Regulated superannuation funds

3.142 Some submissions argued that the particular characteristics of regulated superannuation funds mean that they should be considered differently to many other services for the purposes of the AML/CTF regime; that is, they should not be subject to the same stringent requirements as those services that are considered to be high-risk.

3.143 Insurance Australia Group (IAG) suggested that:

> Given [superannuation contributions] are statutory contributions that cannot be withdrawn prior to retirement there is an extremely low risk of money laundering.[134]

3.144 IFSA supported the position that superannuation should be considered low-risk. It argued that:

> These products contain a number of important features that ensure they are neither suitable nor likely to be used by individuals seeking to launder money or finance terrorism.[135]

3.145 ISFA also noted that '[s]uperannuation is specifically mentioned in paragraph 12 of the Interpretive Notes to FATF Recommendation 5 as an example of a low risk

134 *Submission 11A*, p. 5.

135 *Submission 2*, p. 5.

product for which simplified or reduced customer due diligence measures may be appropriate.'[136]

3.146 In addition, The Association of Superannuation Funds of Australia (ASFA) argued that:

> It is when the benefit is actually paid out of the superannuation system or when the member asserts control over their interest, rather than when contributions are received by the fund, that particulate risks arise and customer identification is required.[137]

Self-managed superannuation funds (SMSFs)

3.147 A self-managed superannuation fund has less than five members and the trustee and members are generally the same people. Self-managed super funds are regulated by the ATO rather than the Australian Prudential Regulation Authority (APRA), which are responsible for regulated superannuation funds.

3.148 Advice to the committee was that self-managed super funds present a higher risk profile in terms of AML/CTF than other regulated superannuation funds. Nevertheless, the application of the proposed regime to SMSFs would not be without its challenges.

3.149 IFSA stated that:

> Given the greater control and flexibility allowed to members of SMSFs, these schemes lack a number of the features which make regulated superannuation products low risk.[138]

3.150 The submission provided by CPA Australia and The Institute of Chartered Accountants in Australia highlighted the practical issues created by the Exposure Bill for self-managed super funds. They submitted that:

> In practical terms the Bill would require a trustee to perform Customer Due Diligence on themselves, implement an AML/CTF Program and possibly report on suspicious matters arising out of their own actions.[139]

3.151 AFSA also pointed out that:

> The large number of difficult-to-supervise entities and the potential for collusion between the trustee and member (who are usually the same person) may represent a risk for money laundering and terrorist financing, but, if that is the case, the provision in the Bill requiring customer information and AML/CTF Programs do not work for this group. Although

136 *Submission 2A*, p. 4.

137 *Submission 28*, p. 4.

138 *Submission 2*, p. 6.

139 *Submission 7*, p. 3.

> self-managed funds represent a particular challenge to any AML/CTF system, in the interest of competitive neutrality they should not be exempted from the AML/CTF regime.[140]

Threshold transaction reporting

3.152 ASFA argued that the threshold transaction reporting requirement would significantly impact on superannuation funds. It argued that the proposed reporting threshold could require superannuation administrators to report every transfer, rollover or benefit payment over $10,000 and this 'would be inappropriate for superannuation funds'.[141]

3.153 ASFA noted that:

> The tax-free threshold (which represents a modest benefit) for superannuation is $129,751. $10,000 is a very low amount for superannuation benefits – which are often taken as a lump sum.[142]

3.154 ASFA went on to suggest that:

> The proposed $10,000 threshold for reporting a transaction is too low for superannuation contributions, rollovers, transfers and benefit payments, if all such payments are captured. It may also be too low for reporting of contributions in some funds and in some situations. The need to report a transaction could be risk-based and ways that funds might put this into operations should be explored.[143]

AML/CTF Programs

3.155 ASFA advised that '[b]y 1 July 2006, all superannuation fund trustees other than self-managed superannuation funds (SMSFs) will be licensed under new APRA licensing requirements'.[144] Therefore:

> [I]n this context, AML/CTF Program requirement appear too prescriptive and fail to recognise how APRA-regulated superannuation fund trustees already manage risk.[145]

3.156 ASFA suggested that regulated superannuation funds should be able to integrate the AML/CTF Program requirements into the existing regulatory requirements.

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140 *Submission 28*, p. 8.

141 *Submission 28*, p. 5.

142 *Submission 28*, p. 5.

143 *Submission 28*, p. 5.

144 *Submission 28*, p. 6.

145 *Submission 28*, p. 6.

Casinos/clubs

3.157 The Exposure Bill lists the provision of 'a gambling service, where the service is provided in the course of carrying on a business'[146] as a designated service. Therefore, AML/CTF obligations are imposed on businesses operating in the gaming industry.

3.158 The committee heard that there are key differences between the gaming industry and the financial services industry. As a consequence, some of the AML/CTF obligations may not necessary and, if imposed, may negatively impact on the effective procedures that are currently in place or result in higher operational costs.

3.159 The committee received evidence from Clubs Australia, representing registered and licensed clubs, and the Australian Casino Association (ACA) which represents the casino operators of Australia.

Casinos – customer due diligence

3.160 Mr Chris Downy from the ACA argued that '[f]rom both a consumer's perspective and a business perspective, gambling is fundamentally different from the services provided by financial institutions'.[147] The ACA highlighted the proposed customer due diligence regime as an area where there is substantial difference between the two industries.

3.161 Mr Downy argued further that:

> The vast majority of casino customers are small recreational gamblers, typically occasional customers, who are no different from customers of restaurants or other entertainment services. To attempt to identify their transactions, record them, data match them or otherwise track them makes no sense because it is almost inconceivable that they are associated with money laundering or terrorism financing.[148]

3.162 Mr Anthony Seyfort, also for the ACA, continued:

> … at the moment we simply do not know the vast majority of people who come in once in a blue moon and spend a tiny amount of money, and there are thousands and thousands of those people … [W]e have a problem with the whole part 2 of the bill – simply this concept in the bill at the moment that you have to know every customer, full stop, whether they are suspicious, large or whatever.[149]

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146 Proposed table 2, section 6.

147 *Committee Hansard*, 14 March 2006, p. 23.

148 *Committee Hansard*, 14 March 2006, pp 23-24.

149 *Committee Hansard*, 14 March 2006, pp 25-26.

3.163 Mr Downy raised an additional issue with respect to the obligation in the Exposure Bill that casinos must obtain detailed information about high-risk customers. Current legislation already requires that casinos report the activities of high-risk customers to AUSTRAC. Casinos may also be required to provide ongoing assistance to any review of these activities.[150]

3.164 The ACA suggested to the committee that the system that is currently in place works well and should be incorporated into the Exposure Bill.

Casinos – safe harbours

3.165 Mr Downy also advised the committee that members of the ACA fear the consequences, under statute and civil law, if despite their best efforts, they fail to comply with 'a complex and unwieldy set of requirements'.[151] He also submitted that:

> It is also very unclear how a broadly cast program required by a federal law would reconcile with the obligations of the specific state statutes such as the Casino Control Act if there were some inconsistency.[152]

3.166 Mr Downy suggested that 'the draft exposure bill could be amended to ensure that nothing casinos do in lawful compliance with their respective state based obligations would constitute non-compliance with the draft exposure bill'.[153]

Registered/licensed clubs

3.167 The Exposure Bill acknowledges that not all industries will pose the same level of risk in terms of money laundering or terrorism financing. Proposed section 28 provides identification procedures for certain low-risk services.

3.168 Clubs Australia argued that clubs already have player verification procedures in place and that the highly regulated gambling environment means that 'the imposition of any additional identification requirements to address risk cannot, in our view, be justified'.[154]

3.169 Clubs Australia also highlighted that electronic gaming machines are required to be connected to a centralised monitoring system. The submission went on:

> State Governments already have full access to EGM performance data which in our view is capable of identifying suspicious EGM activity if appropriate data analysis techniques are applied. Clubs Australia again notes that the cost of collecting this data is already borne by the clubs and

150 *Committee Hansard*, 14 March 2006, p. 24.

151 *Committee Hansard*, 14 March 2006, p. 24.

152 *Committee Hansard*, 14 March 2006, p. 24.

153 *Committee Hansard*, 14 March 2006, p. 24.

154 *Submission* 6, p. 2.

> the imposition of additional costs as a result of the proposed legislation is not in our view warranted.[155]

3.170 In conclusion, Clubs Australia argued that:

> It is our view that the gambling environment in clubs already poses a very low risk in the context of money laundering and terrorist financing and that … clubs should be excluded from the AML/CTF legislation.[156]

Financial planners

3.171 Currently, proposed section 6 lists personal advice given by a licensed financial planner in relation to securities and derivatives, life policy or sinking fund policy, superannuation funds or retirement savings accounts as a designated service.

3.172 The issue of whether the provision of financial advice should be listed as a designated service for the purpose of the AML/CTF regime was raised with the committee.

3.173 The FPA argued that:

> There does not seem to be any convincing reasons why the provision of financial advice in itself should trigger the AML/CTF obligations. The obligation for financial planners should instead rest on actions taken to implement their client's strategy.[157]

3.174 The FPA highlighted that the practical affect of the regime would result in customers having to identify themselves each time they consult with a financial planner. This may not sit comfortably with general advice from authorities such as ASIC that consumers consult with a number of planners before finalising their decision.[158]

3.175 Mr John Anning of the FPA acknowledged that:

> It may be the practices of financial planners would be better served if they did the identification up-front, at the initial contact with the client. But we believe that is a flexible point, and that they should be able to decide for themselves.[159]

3.176 The FPA suggested that 'it is highly unlikely that identification at the advice stage would result in greater benefits in terms of AML/CTF intelligence than

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155 *Submission 6*, p. 3.

156 *Submission 6*, p. 4.

157 *Submission 24*, p. 5.

158 *Submission 24*, p. 5.

159 *Committee Hansard*, 14 March 2006, p. 17.

identification at the implementation stage'[160] and, as such, favoured the position that the provision of financial advice should not be a designated service.

Sole practitioners

3.177 The APF highlighted that:

> There are many thousands of financial advisers and planners, as well as solicitors and accountants acting in a financial advisory capacity. These advisers – often sole practitioners – will acquire obligations under the law with customer identification, reporting and monitoring requirements which will be extremely onerous both for the service provider and for the customer or client.[161]

3.178 The APF went on to argue the likelihood that:

> The burden and inevitable cost of compliance by small financial advisers and planners [would] have significant implications for the availability and affordability of financial advice at a time when governments are expecting individuals to take increasing responsibility for their financial security. [162]

3.179 The FPA supported this view:

> … it would be clearly impractical for financial planners to bear all of these obligations individually. FPA considers that effective fulfilment of the AML/CTF obligations will require recognition in the legislation of the pivotal role played by the A[ustralian] F[inancial] S[ervices] Licensee in the provision of financial services.[163]

Department response

3.180 In relation to some of the issues raised in relation to financial planning (and accountants), a representative from the Department told the committee that:

> The financial planners are picked up in table 1 if they provide specific product advice, but they are not if they provide general advice. The concept was that they are gatekeepers, so let us bring in the regulations and the rest of it at an early point. They have raised the question of whether, one, it is appropriate and whether, two, it is feasible, and the problems that it poses to their members to suddenly take off one hat and put on another and then require a person to provide identification material. Again, we have heard that. The accountants for the most part will be caught up in the second tranche of this legislation, because that is where we will have to grapple with how we regulate a lot of industry sectors that have not formerly been

160 *Submission 24*, p. 5.

161 *Submission 4*, p. 5.

162 *Submission 4*, p. 6.

163 *Submission 24*, p. 5.

> regulated. One of the issues that will be looked at in the wash-out after the consultation period is whether those provisions remain in table 1.[164]

Insurance

3.181 General insurance is not listed in the Exposure Bill as a designated service. Many organisations supported the exemption of general insurance from the AML/CTF regime.

3.182 The Insurance Council of Australia (ICA) stated that:

> ICA supports the exclusion of general insurance from the proposed legislation … [I]t is our recommendation that the proposed exemption of general insurance is maintained.[165]

3.183 Insurance Australia Group (IAG) expressed a similar view:

> IAG agrees with the assessment of the Australian Attorney General's Department that general insurance should not be a designated service, due to its extremely low risk nature, an assessment that is consistent with the FATF recommendations.[166]

3.184 However, IAG noted an unintended consequence of the Exposure Bill with respect to insurance:

> As an A[ustralian] F[inancial] S[ervices License] holder, a general insurer could be authorised to provide financial product advice in relation to life products, limited life risk insurance products and any products issued by a registered life insurance company relating to C[onsumer] C[redit] I[nsurance] products. Based on the AFSL authorisations, the general insurer would be deemed to be providing a designated service if it provides personal financial product advice. IAG submits that this is an unintended consequence of the Draft Exposure Bill.[167]

Life Products

3.185 Life products can be divided into two broad categories:

- life risk products; and
- investment life products.

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164 *Committee Hansard*, 14 March 2006, p. 75.

165 *Submission 30*, p. 2.

166 *Submission 11A*, p. 3.

167 *Submission 11A*, p. 5.

3.186 Commonly both products are referred to as life insurance but 'the two classes of product must be carefully distinguished as they can present very different AML/CTF profiles'.[168]

3.187 IFSA highlighted that life risk insurance products share most of the characteristics of general insurance and therefore suggested that 'most life risk insurance products present a minimal to low money laundering risk'.[169]

3.188 In contrast, investment life products are or can be used for investment purposes. IFSA stated that:

> Such products have a surrender value, are transferable, can be used as collateral of a loan and can have high, lump sum premiums and payouts. As a result, and subject to some exceptions … these products can be considered to be medium risk and require a greater level of due diligence than life risk products.[170]

3.189 IFSA submitted that life risk insurance; life products acquired by superannuation funds; and life products having an annual premium of no more than A$1,500 or a single premium of no more than A$4,000 generally present a low to minimal risk of money laundering and should be classified by the Rules as low risk designated services for the purposes of proposed section 28 of the Bill.[171]

3.190 IFSA also suggested that a similar level of customer due diligence as applies to other investment products may be appropriate for investment life products not identified as low risk.[172]

Committee view

3.191 The committee applauds the extent and nature of the ongoing consultations between the Minister, the Department and AUSTRAC, and business and industry groups in relation to the proposed AML/CTF regime. However, the committee shares concerns that, without the full package of draft legislative instruments, affected industry bodies are unable to analyse sufficiently the full impact of the regime on their business operations. Since much of the detail of the regime is contained in the Rules, **the committee believes it is imperative that the complete set of Rules be released for comment prior to the final version of the bill being introduced into Parliament**.

168 IFSA, *Submission 2A*, p. 6.

169 *Submission 2A*, p. 7.

170 *Submission 2A*, p. 8.

171 *Submission 2A*, p. 9.

172 *Submission 2A*, p. 11.

3.192 In stating this, the committee is aware that development of the Exposure Bill and its associated documentation is an evolving process, and that the bill to be introduced into Parliament can be expected to differ from the publicly-released version which has been the subject of this inquiry. The committee is encouraged by assurances from the Department that it will continue to work closely with stakeholders to ensure that outstanding contentious issues and concerns will be resolved prior to the bill's introduction into Parliament.

3.193 Accordingly, and cognisant of the fluid nature of the process, the committee has used its inquiry as a vehicle for concerns to be aired and debated. The committee does not consider it appropriate, and is not inclined, to make recommendations in relation to technical aspects of the Exposure Bill as it currently stands. Rather, **the committee strongly encourages the Minister, the Department and AUSTRAC to utilise the expertise and knowledge of industry bodies to ensure the measures in the final AML/CTF package are truly risk-based, in order to reflect and promote business efficacy.** This is particularly important given that there appears to be a significant divergence between the Department and AUSTRAC, on the one hand, and industry, on the other, about what the term 'risk-based' actually means and whether the Exposure Bill encompasses a risk-based approach. The committee encourages the Department and AUSTRAC to work more closely with industry in order to achieve greater consensus in relation to the meaning and application of a risk-based approach.

3.194 **The committee also encourages the adoption of a realistic and workable timeframe for implementation of the new regime to allow business to undertake appropriate system changes**. The committee acknowledges the concerns expressed by many submissions and witnesses with respect to timing issues, particularly given the staggered and late release of the Rules. Accordingly, **the committee also encourages an extension of the consultation period to accommodate those concerns and to ensure effective consultation on any residual matters**. The committee notes that, at the time of writing (11 April 2006), the outstanding Rules are yet to be released publicly. This is of particular concern given that a period of at least five or six weeks from the date of delivery of the Rules was nominated by many groups as a minimum timeframe for analysis and completion of detailed submissions to the Department's consultation process.