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8 March 2006

Jonathan Curtis
Committee Secretary
Senate Legal and Constitutional Legislation Committee
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Parliament House
CANBERRA ACT 2600
AUSTRALIA

Email: LegCon.Sen@aph.gov.au

Dear Mr Curtis

Inquiry into the Exposure Draft of the Anti-Money Laundering and Counter-Terrorism Financing Bill 2005

The Institute of Chartered Accountants in Australia (the Institute) and CPA Australia appreciate the opportunity of providing the Senate Legal and Constitutional Legislation Committee their views on the *Anti-Money Laundering and Counter-Terrorism Financing Bill 2005* (the Bill) which was referred to the Senate on 9 February 2006. The Institute and CPA Australia look forward to meeting with the Committee to provide any further information that may be required.

Support for Anti-Money Laundering/Counter-Terrorism Financing (AML/CTF) Reform

The Institute and CPA Australia support the objectives of the Financial Action Taskforce (FATF) Recommendations and have worked with government throughout the consultation process leading up to the release of the draft Bill.

The Institute and CPA Australia were encouraged by the public statements prior to the release of the draft Bill committing the government to the adoption of a risk-based approach. A copy of the Joint Communiqué issued by the Minister for Justice and Customs on 15 September 2005 is attached.

Regulatory process

The government has regularly confirmed its commitment to improving the regulatory environment for business and to cutting red tape. Despite this stated commitment our consultations with the Attorney-General's Department and AUSTRAC to date suggest that the pre-regulatory development process is not adequately factoring in commercial realities and the practicalities of undertaking business in Australia. We believe the process will deliver complex, over-burdensome regulation for the following reasons:

- Rushed process – after two years of consultation the government released a draft Bill in December last year with the aim of introducing the Bill into Parliament in June. While a four month time-frame for comment would be adequate in most circumstances, the majority of the related rules and guidelines, which provide the detail on compliance processes and obligations, have not yet been released and many have not yet been drafted;

- Expansiveness – the scope of the bill extends far beyond the government's FATF requirements seeking to capture as broad a range of transactions as possible, despite the promise of a risk-based approach. There appears to be little willingness to balance the risk of money laundering against the impact on business and the general public in terms of inconvenience and compliance costs.

  We had been advised that the first tranche of the Bill will only impact on the financial services sector and businesses in competition with the sector, however the definitions of designated services are so broad that they currently cover all businesses which provide trade credit. It is our understanding that all consumer credit transactions will also 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.

- Not a risk-based approach - The Bill purports to represent a risk-based approach but is in fact overly prescriptive. Unless the AML/CTF reform is targeted at the highest risk transactions it will impose an unnecessary compliance burden, particularly on small businesses. The prescriptive nature of the Bill and draft Rules is also inconsistent with the FATF Recommendations.

- Lack of materiality - Only one 'designated service" in the Bill (the issuing of stored value cards) has a financial threshold. All other services have no thresholds at all. For example, issuing any postal order will trigger minimum customer identification procedures. Is it the intention of the government that those people without cheque accounts who use postal order for small personal transactions will be required to go through an identification process? This reflects an unnecessary 'catch-all' approach without consideration of the flow on impacts

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.

A number of specific concerns with the Bill are outlined below.

Scope of the Bill

Definitions

Clause 3 of the Bill states that the object of the Act is the fulfillment of Australia's international obligations including the FATF Recommendations, which are intended to prevent the use of the financial system for the purpose of money laundering and terrorist financing. These obligations are defined in clause 5 as being the 'Revised' Forty Recommendations adopted by FATF on 20 June 2003 and Special Recommendations on Terrorist Financing adopted on 31 October 2001 and 20-22 October 2004.

The 'Overview of the exposure Anti-Money Laundering and Counter-Terrorism Financing Bill' states that services provided by accountants are only to be brought into the scope of this first tranche of AML/CTF reforms to the extent that those services are provided in direct competition with the financial sector, implementing the FATF Recommendations as they relate to a range of services primarily provided by financial institutions, the gambling sector and bullion dealers.

The descriptions of certain designated services in clause 6 of the Bill go far beyond the FATF Recommendations and seem to extend the application of the Bill to services which are not in direct competition with the financial sector.

In particular the following definitions are extremely broad and unworkable in their current form.

(a) The definition of 'loan' at clause 5 is very broad and includes 'the provision of credit or any other form of financial accommodation'. This definition should be limited to loans provided by a person or entity who conducts as a business the providing of loans. The definition in clause 6, Item 6 of the Bill of 'making a loan, where the loan is made in the course of carrying on a business' could extend the application of the Bill to any business which provides any loan or provides its goods or services to customers on any terms of credit. This would include accountants who allow their clients to pay for accounting services on a deferred payment basis.

(b) The phrase 'carrying on business' is widely used in clause 6. Together with the definition of 'business', as used in the description of designated services in clause 6, it is unqualified so that it applies to any type of business regardless of whether it is a business of providing financial services or banking. However, the FATF Recommendations are expressed to impose obligations on 'financial institutions', being 'any person or entity who conducts as a business one or more' of the prescribed activities. 'Business' should be defined in the Bill so as to limit its application to those designated services provided by 'financial institutions' or their competitors.

Designated services

Self-Managed Superannuation Funds (SMSFs)

The trustee of a superannuation fund will become a reporting entity by virtue of providing a designated service listed in Items 46 and 47 in Table 1 of clause 6 of the Bill.

There are several characteristics of SMSFs which are relevant to the AML/CTF compliance obligations which would be imposed on the trustee of a SMSF.

- All trustees of a SMSF must also be the beneficiaries of the fund.
- The maximum number of trustees/beneficiaries in a SMSF must be less than five and those members must be related or be in a business relationship.
- SMSFs must be audited annually both in relation to their compliance with accounting standards and the SIS requirements.
- SMSFs are regulated by the ATO.
- Although participating in the structure of the SMSF provides a tax benefit to the member, the SMSF itself is not the provider of a financial service to a third party.

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.

The SMSF will become a consumer of financial services when the members' funds are invested in cash products, managed funds, direct equities or real estate. At this point the identity of the trustees and beneficiaries of the funds and the source of funds will be subject to AML/CTF procedures of the financial institutions as AML/CTF reporting entities.

Reporting of suspicious offences

There is no limitation on the predicate offence in the Bill. During our earlier consultation with the Attorney General's Department, we were led to believe that it was the intention that the legislation should apply only to serious offences, being indictable offences rather than all offences.

The Bill imposes a requirement in clause 39 that a reporting entity must report to AUSTRAC where it has reasonable grounds to suspect that it has information which may be relevant to, among other matters, the investigation of, or prosecution of a person for, an offence against a law of the Commonwealth or of a Territory.

The international efforts to combat money laundering and terrorist financing require global cooperation and consistency between jurisdictions as recognized in the FATF Recommendations and the Third European Union Directive.
The FATF Recommendations set out twenty of the 'designated categories of offences' which constitute the serious offences to which the crime of money laundering should apply. These range from participation in organized criminal group and racketeering to extortion and fraud.

The Third European Union Directive, issued in October 2005, requires member countries to ensure the consistency of their definitions of the serious crimes which will be predicate offences for money laundering and terrorist financing legislation. These predicate offences are to be 'all offences which are punishable by deprivation of liberty or a detention order for a maximum of more than one year or for those states which have a minimum threshold for offences in their legal system, offences punishable be deprivation of liberty or a detention order for a minimum of more than six months.'

In the UK where reporting obligations under the Proceeds of Crimes Act 2002 has extended to all crimes, the large volume of reporting led the National Criminal Intelligence Service to establish a parallel system for reports of 'Lesser Intelligence Value' which are largely ignored. It would seem preferable to focus the resources of the reporting entities and the regulators on significant and organized crime by limiting the predicate offences to indictable offences.

Impact on SMEs

An ABS Survey of Accounting Practices in 2001-2002 showed that 97% of accounting practices in Australia were businesses with less than five principals with 67% being sole principal practices. The view that this Bill will only impact on businesses in competition with the financial services sector is flawed. Many small businesses will be caught under this Bill and it is essential to ensure that the compliance regime outlined in the Rules will be flexible enough to allow reporting entities to tailor their approach to compliance having regard to the nature, scale and complexity of the business that they operate. Given the scope of the Bill, the rules should not be drafted to best suit large organizations with comprehensive resources at their disposal.

The Bill will impose significant new obligations on the professional services sector in which it is common to operate trust accounts in which client funds are held. The AML/CTF compliance costs for these businesses will be significant. It is vital that the legislation targets high-risk clients, services and transactions in order to achieve the purpose of the legislation while at the same time minimising the compliance burden on SMEs.

It does not represent an efficient use of resources to impose the same obligations on accounting practices, which are likely to be SMEs, as are imposed on large financial institutions which have existing AML systems and reporting requirements under the Financial Transactions Reports Act.

Because of the limited resources available to these small entities, it would only be economically justifiable to implement customer identification procedures, and AML/CTF Program and provide reports regarding suspicious matters where those obligations relate to clearly defined, high risk customers, transactions and/or jurisdictions.

In many cases, the obligations imposed in the Bill on the accountants providing designated services will represent an additional layer of compliance obligations and a duplication of AML/CTF procedures. The clients of an accountant would, other than in exceptional circumstances, already hold accounts and acquire products through financial institutions. These clients would have previously been subjected to the customer identification procedures of these other reporting entities.

Risk based approach

Customer due diligence

While the Bill purports to be principles-based, there are significant areas where prescriptive requirements have replaced this risk-based approach.

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.

Clause 35 only allows 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.

For example, a transaction processed through an accountants trust account might be related to an Australian Tax Office refund which is then transferred directly to the client. Despite the low risk nature of the individual transaction, the full identification obligations in Part 2 of the Bill and the AML/CTF Rules would be required.

Third Party verification

The arrangements in the Bill relating to third party verification of customer identification are not workable in relation to the services provided by accountants.

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.

This will lead to unnecessary duplication of the resources required of both the accountant as reporting entity and the customer in performing these applicable customer identification procedures.

In a survey of members, 76% of the respondents identified that 90-100% of their clients had existing relationships with banks and/or financial institutions. The Bill should allow accountants to place some reliance on the customer identification procedures conducted by the financial institutions and government agencies.

Clear efforts have been made in the drafting of the Bill to ensure that only those documents which are considered sufficiently robust be considered suitable as primary and secondary identification documents. However, the result is to limit the primary and secondary documents which can be used to complete the applicable customer identification procedure, leading to unnecessary duplication of customer identification by government agencies and industry and thereby increasing the costs to industry. It would be preferable to address the issues within government which undermine the usefulness of the documents issued by government agencies which have conducted the identification procedures.

Exclusion from tipping off requirements

Clause 95 of the Bill provides an exclusion from the 'tipping off' prohibitions for a legal practitioner who makes the disclosure in relation to the evasion of a taxation law. As accountants as well as lawyers are involved in the area of taxation services it is appropriate that this exclusion be extended to accountants to ensure that the legislation is competitively neutral.

Consultation process

We have concerns that it will not be possible to provide an adequate response in relation to the Bill by 13 April 2006 due to the complexity of the legislation and the lateness of the release of the supporting AML/CTF Rules.

In the area of customer identification procedures, AUSTRAC have not yet released the following Rules:

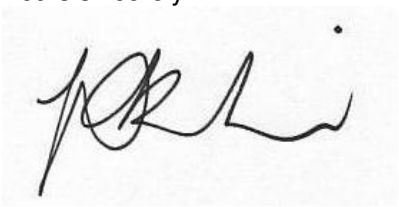
- Pre commencement customer – continuity of relationship
- Rules for identification of companies, trusts and partnerships
- Rules re Risk trigger events
- Third party identification procedures
- Non face-to-face identification procedures
- Customer identification procedures in 'special circumstances'.

In order to determine the extent to which the Bill will impact on the professional services sector, CPA Australia and the Institute have undertaken a number of activities including:

- An online survey and collection of Quality Review data to gauge the extent to which accountants currently provide designated services;
- Taskforce to identify the implications of compliance requirements as set out in AML/CTF Rules for members in practice.
- Focus groups to work though the risk issues and likely compliance costs; and
- Legal advice to be obtained as issues arise

We would be pleased to provide the Committee with the outcomes of these activities once they have been undertaken.

Yours sincerely



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