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Dear Ms Dennet

**Inquiry into the Financial Transaction Reports Amendment
Bill 2006**

We thank you for the invitation to comment on the Financial Transaction Reports Amendment Bill 2006. We enclose our submission. We have referred throughout the submission to the Draft Exposure Anti-Money laundering and Counter Terrorism Financing Bill 2005. For the avoidance of doubt those references are to the 1st Draft Exposure Bill released in December 2005.

Yours faithfully

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Submission to the Senate Legal and Constitutional Committee on the Inquiry into the Financial Transaction Reports Amendment Bill 2006

1. Introduction

The Financial Transaction Reports Amendment Bill 2006 (*the Bill*) is proposed to amend Division 3A of the Financial Transaction Reports Act (*the FTRA*). Division 3A was introduced to bring the Australian AML/CTF regime into compliance with FATF Special Recommendation VII (*SRVII*) and was enacted by Schedule 9 of the Anti-Terrorism Act No 2 2005(Cth). It does not come into force until 14 December 2006.

The request for submissions received from the Acting Committee Secretary indicated that the Bill has been introduced to rectify certain difficulties identified by non-bank remitters in the first consultation period on the Draft Exposure Anti-Money Laundering and Counter Terrorism Financing Bill 2005 (*the AML/CTF Bill*).

A recent media release from the Australian Financial Markets Association indicated the amendments in question were requested by the finance sector because parts of the amended FTRA did not align with the proposed new AML/CTF Bill (thereby necessitating two system changes, to meet new FTRA requirements in December 2006 and subsequently the new AML/CTF law).

In summary the Bill:

- amends the definition of "account" in the FTRA but only for the purposes of Division 3A;
- restricts the application of Division 3A to ADIs (*authorised deposit taking institutions*¹). At the moment it applies to "cash dealers";
- clarifies what is meant by "customer identification" for outgoing International Funds Transfer Instructions (*IFTIs*) and amends the definition of "customer identification" for incoming IFTIs.

References throughout this submission to the AML/CTF Bill are to the 1st Draft Exposure Bill released in December 2005. It may be that some of the difficulties we have identified will be resolved in the revised Bill which is due to be released soon.

2. Background. Special Recommendation VII

Section 17FA of Division 3A was introduced to bring the Australian AML/CTF regime into compliance with SRVII.

¹ defined in the FTRA as

- (a) a body corporate that is an ADI for the purpose of the Banking Act 1959; or
- (b) the Reserve Bank of Australia; or
- (c) a person who carries on State banking within the meaning of paragraph 51(xiii) of the Constitution

In summary, SRVII requires financial institutions (who are defined using the broad FATF definition) to include meaningful and accurate originator information (ie, name, address and account number) on funds transfers and related messages that are sent by one financial institution to another financial institution. The information should remain with the transfer or related message through the payment chain.

Section 17FB was introduced to comply with Article 14 of the Interpretative Note to SRVII, which requires beneficiary financial institutions to have in place effective risk-based procedures to identify wire transfers (domestic and cross border) that are lacking in complete originator information.

3. Submission 1

3.1 Summary

If the scope of Division 3A is restricted to ADIs it will not be in compliance with SRVII and will be inconsistent with the AML/CTF Bill. The difficulty identified by the Explanatory Memorandum (*the EM*) could be resolved by the amendment of the definition of an IFTI to include only multiple institution instructions.

3.2 Background

The proposed amendment omits the reference to "cash dealer" throughout Division 3A of the FTRA and substitutes the term "ADI". The EM indicates this is to resolve problems arising from the application of the Division to non-bank money remittance businesses. The FTRA does not presently differentiate between non-bank same institution and non-bank multiple institution IFTIs and it is impracticable to require IFTIs sent from one institution in one country to the same institution in another country to include originator information (as it would be passing information to itself).

3.3 Section 17FA.

We submit that the application of section 17FA to ADIs only will result in non-compliance with SRVII.

Article 3 of the Interpretative Note to SRVII applies SRVII to cross-border and domestic wire transfers *between* financial institutions (emphasis added). "Financial institutions" are widely defined in the Forty Recommendations as any persons or entities who conduct as a business one or more of a number of activities or operations for or on behalf of a customer. The activities relevantly include:

- acceptance of deposits and other repayable funds from the public;
- the transfer of money or value;
- issuing and managing means of payment (e.g. credit and debit cards, cheques, traveller's cheques, money orders and bankers' drafts, electronic money); and
- money and currency changing.

It is clear from this list that the scope of SRVII extends beyond ADIs and in particular applies to all institutions that originate, receive or are intermediaries in a wire transfer chain. These would

include non-bank remitters (for example a money remitter who sees the customer and then sends the transfer, even if it uses banking channels, should comply with SRVII).

As presently drafted the obligation in section 17FA applies to "cash dealers" (defined sufficiently widely in the FTRA to include non-bank remitters and remittance services) and is compliant with SRVII.

However the proposed amendment to restrict the application of the section to ADIs will mean that the obligation does not apply at all to non-bank remitters and importantly that remittance services will no longer be included. Consequently Section 17FA (which was introduced so as to bring the Australian regime into compliance with SRVII) will no longer be compliant with that Recommendation.

As a practical alternative we suggest the difficulty identified in the EM could be resolved if the definition of an IFTI in the FTRA was amended to include only multiple institution transfers.

This is all that is required by Article 3 of the Interpretative Note. This would also be consistent with the FATF definition of a wire transfer (as defined in Article 2 of the Interpretative Note). Section 17FA would therefore be compliant with SRVII.

It would also ensure consistency between section 17FA (and section 17FB) of the FTRA and their counterparts, sections 58(6) and 59 of the AML/CTF Bill (which only apply to multiple institution transfers).

3.4 Section 17FB

The same difficulty arises if section 17FB (which deals with incoming IFTIs) is amended so as to apply only to ADIs. This section was introduced to comply with the requirements of Article 14 of the Interpretative Note (that beneficiary institutions should have in place risk-based procedures for identifying and handling wire transfers that are not accompanied by complete originator information).

As presently drafted the obligation, which does apply to cash dealers, is compliant with SRVII but if, as is suggested, it is restricted to ADIs it will not apply at all to non-bank remitters and remittance services and will no longer be compliant.

3.5 Inconsistencies with the AML/CTF Bill

Additionally we submit that the substitution of "cash dealer" by "ADI" in sections 17FA and 17FB will lead to inconsistency between those sections and their counterparts, sections 58(6) and 59 of the AML/CTF Bill.

Section 58(6) imposes a comparable requirement to section 17FA in that it requires persons involved in a multiple-institution funds transfer chain to include customer information on outgoing funds transfers instructions. The persons required to comply with section 58(6) are not restricted to ADIs. They include any persons in the funds transfer chain (ie, originating and destination institutions (who themselves need not be ADIs) and any persons interposed between).

In the same way there will be an inconsistency between the scope of section 17FB of the FTRA and section 59 of the AML/CTF Bill (which applies to "destination institutions").

If the proposal, (suggested above) to amend the definition of an IFTI in the FTRA to include only multiple institution transfers were adopted these inconsistencies would be resolved.

3.6 Inconsistencies with Division 3 of the FTRA

The proposed amendment will also lead to an inconsistency between Division 3 (the obligation to report incoming and outgoing IFTIs to AUSTRAC) and Division 3A of the FTRA in that IFTIs will be treated differently depending on whether they are sent or received by cash dealers or ADIs. For example all cash dealers will need to make an AUSTRAC report (pursuant to section 17B of Division 3) but only those cash dealers who are ADIs will have to include originator information with the IFTIs (pursuant to section 17FA).

The EM appears to suggest that reporting to AUSTRAC may be sufficient for non-ADIs to satisfy SRVII. Clearly it does not.

4. Submission 2

4.1 Summary

The amendment to the definition of "customer information" in section 17FA may mean that section is no longer compliant with the Interpretive Note to SRVII. The Government may wish to clarify the position with the FATF Secretariat before proceeding further.

We suggest as a practical alternative that the language of section 67(c) and (d) of the AML/CTF Bill be adopted. This would have the advantage of consistency and section 67 is in compliance with SRVII. (This assumes section 67 of the AML/CTF Bill will remain in the same terms in the next draft, as the object of consistency between the FTRA and the AML/CTF Bill will not be achieved otherwise.)

4.2 Section 17FA

The Bill amends the definition (in section 17FA) of the "customer information" to be included with an outgoing IFTI instruction to include:

- (a) the ordering customer's name and full business or residential address; and
- (b) either
 - (i) if the IFTI is to be transmitted from a single account held by the customer with the ADI, the account number; or
 - (ii) in any other case, the identification code assigned to the instruction by the ADI.

The amendment is intended to clarify that an account number is only required when the instruction relates to transferring money directly from a single account with the ADI. In all other cases an ID code is permitted instead of an account number.

The EM explains this is to make it clear that either an account number or an identification code can be used (some customers will not be account holders). However the EM goes further and says that as in practice financial institutions transmit multiple numbers of IFTIs in batch form (even if some or all are on behalf of account holders) it is more practical to use an ID code to cover all those transmitted in a particular batch. That suggests that the required identification number need not be unique, and the Bill does not specify that the identification number must be unique to an instruction.

Although this amendment seems practical we are concerned that section 17FA as amended will not comply strictly with SRVII. Article 5 of the Interpretative Note requires information accompanying cross border wire transfers to include name, address and, where an account exists, the number of that account. It is only in the absence of an account that a unique reference number can be used. (It should be noted there is an inconsistency between Article 5 and the FATF Evaluation Methodology which permits the use of an unique reference number if no account number exists).

Article 7 of the Interpretative Note does permit either the use of an account number or a unique reference number but only applies where a number of individual transfers from a single customer are batched (and the batch file itself contains full originator information that is fully traceable in the destination country).

In summary therefore, according to FATF, it is only where:

- there is no account; or
- there is a batched file from a single customer,

that the financial institution has the choice whether to use an account number or a unique reference number.

The proposed amendment goes further than this by permitting financial institutions to use either in most circumstances² and by allowing the identification number to be one relating to the batch of which the transaction forms part where the batch might include transactions for a number of different customers.

If the AML/CTF Bill stays in its current form then financial institutions will need to make two systems changes in order to comply with the FTRA changes and another to comply with the new AML/CTF law. We understand one of the objectives of the Bill is to avoid this (although financial institutions could in practice avoid this by adopting from the start unique identifiers for each transaction even if the transaction is batched).

We note that the European Commission proposed Regulation on Payer Information Accompanying Wire Transfers (which the European Parliament has agreed at first reading and which can be found at

<http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/1008&format=HTML&aged=1&language=EN&guiLanguage=en>) adopts the FATF approach and permits a unique identifier to be used only when an account number does not exist where funds are transferred to payees outside the European Community (except in the case of batch file transfers from a single payer).

5. Submission 3

5.1 Summary

The amendment to the definition of "customer information" in section 17FB may mean that section is no longer compliant with the Interpretative Note to SRVII. The Government may wish to clarify the position with the FATF Secretariat before proceeding further.

² except if the IFTI is to be transmitted from a single account held by the customer with the ADI,

We suggest as a practical alternative that the language of section 67(c) and (d) of the AML/CTF Bill be adopted. This would have the advantage of consistency and section 67 is in compliance with SRVII.

5.2 Section 17FB

The Bill amends the definition of "customer information" in section 17FB (which deals with incoming IFTIs).

According to the EM the purpose of the amendment is to overcome the problem faced by Australian ADIs and AUSTRAC in determining whether a customer has an account with a foreign ordering organisation by providing that a customer's account number or identification code have equal standing for incoming IFTIs. The definition of "customer information" in section 17FB now includes, at section 17FB(6)(c), either:

- (i) the number of the customer's account with the ordering organisation; or
- (ii) the identification code assigned to the instruction by the ordering organisation.

We believe that the same difficulty referred to in Submission 2 arises in this case. Article 14 of the Interpretative Note refers to "complete originator information", which only permits the use of a unique identification number where an account does not exist.

6. Submission 4

If the changes we discuss in Submission 1 are made notwithstanding our submission then, to be consistent with those changes, section 29(4)(ba) of the FTRA should be amended from "cash dealer" to "ADI".