Australian Government
Attorney-General's Department

September 2017

Senate Legal and Constitutional Affairs Legislation Committee

Inquiry into the Anti-Money Laundering and Counter-Terrorism Financing Amendment Bill 2017

Attorney-General's Department Submission

Contents

Introduction

The Attorney-General's Department (AGD) thanks the Senate Legal and Constitutional Affairs Legislation Committee for the opportunity to make a submission to its inquiry into the provisions of the Anti-Money Laundering and Counter-Terrorism Financing Amendment Bill 2017 (the Bill).

Our submission has been prepared in consultation with the Australian Transaction Reports and Analysis Centre (AUSTRAC), the Australian Criminal Intelligence Commission, the Australian Federal Police and the Department of Immigration and Border Protection. It sets out additional information regarding the policy rationale for some of the key measures in the Bill, which include:

- applying AML/CTF regulation to digital currency exchange businesses, closing a regulatory gap in the coverage of this emerging industry to mitigate the risks of its misuse and exploitation for the purposes of money laundering or the financing of terrorism
- strengthening the powers of AUSTRAC to supervise the registration of remitters
- giving the AUSTRAC CEO additional and a more efficient means for promoting and encouraging compliance with Australia's AML/CTF laws through the expansion of the infringement notice and remedial direction provisions
- providing regulatory relief to industry, including de-regulating the cash-in-transit sector and clarifying financial institutions' correspondent banking due diligence obligations, and
- giving police and customs officers broader powers to enforce reporting obligations with respect to cross-border movements of physical currency and bearer negotiable instruments.

The statutory review of Australia's AML/CTF regime

The Bill implements the first phase of reforms arising from the report on the statutory review of Australia's anti-money laundering and counter-terrorism financing (AML/CTF) regime (the Report).

Section 251 of the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (AML/CTF Act) required a review of the operation of the regulatory regime – that is, the AML/CTF Act, AML/CTF Regulations and AML/CTF Rules – to commence before the end of the period of seven years after the commencement of that provision. The review commenced in December 2013 and involved an extensive consultation process with industry, civil society and government stakeholders.

While the obligation in section 251 of the AML/CTF Act was limited to the review of the operation of the AML/CTF regime, issues concerning the operation of the *Financial Transaction Reports Act 1988* (FTR Act), which operates in parallel to the AML/CTF Act, were also considered.

The Report was tabled in the Parliament by the Minister for Justice, the Hon Michael Keenan MP, on 29 April 2016. The Report makes 84 recommendations to strengthen, modernise, streamline and simplify Australia's AML/CTF regime, and enhance Australia's compliance with the international standards for combating money laundering and terrorism financing set by the Financial Action Task Force (FATF), an inter-governmental policy-making body.

As a foundation member of the FATF, Australia periodically undergoes a mutual evaluation (or peer review) to assess its compliance with the FATF Recommendations and the effectiveness of its AML/CTF measures. The 2015 mutual evaluation of Australia identified a number of deficiencies and made a number of recommendations to strengthen compliance and effectiveness. These recommendations were taken into account as part of the statutory review.

The review recommendations are being implemented in phases with this Bill implementing the first set of measures. Future phases will progress significant reforms, the detail of which need to be developed in close consultation with Government agencies and industry. These include measures to simplify, streamline and clarify AML/CTF obligations, and further strengthen compliance with the FATF standards.

Regulating digital currency exchange providers

A key feature of the Bill is the application of AML/CTF controls to the digital currency exchange sector. Digital currencies, which have largely operated outside the scope of the regulated financial system, are increasingly being used as a method for the payment of goods and services and transferring value in the Australian economy.

While digital currencies offer the potential for cheaper, more efficient and faster payments, the associated money laundering and terrorism financing risks are well-documented. Key risks include:

- greater anonymity compared with traditional non-cash payment methods
- limited transparency because transactions are made on a peer-to-peer basis, generally outside the regulated financial system, and
- different components of a digital currency system may be located in many countries and subject to varying degrees of AML/CTF oversight.

These are not merely hypothetical risks. In May 2013, the U.S. Department of the Treasury and the Department of Justice undertook coordinated enforcement action against Liberty Reserve, a digital currency system used to facilitate USD 6 billion worth of illicit web-based activity, including identity fraud, credit card theft, online scams, and dissemination of computer malware.[1]

The regulatory regime under the AML/CTF Act dates from 2006 and currently only applies to an ‘e-currency’, which is backed by a physical thing. It excludes convertible digital currencies, such as Bitcoin, which are backed by a cryptographic algorithm.

This regulatory gap is also having an impact on the legitimacy and public perception of the digital currency sector, which may impede developments or the use of these currencies in the future. AGD understands that many existing businesses are concerned about the risks associated with dealing with digital currency and are choosing not to use or accept this payment method. Banks are also concerned about the risks associated with providing services to digital currency businesses, which can limit access to traditional banking services for the digital currency sector.

The Report examined the provisions of the AML/CTF Act that apply to digital currencies and concluded that AML/CTF regulation should apply to digital currency exchange providers. This recommendation was also consistent with the conclusions of the Senate Economics References Committee 2015 report ‘Digital currency – game changer or bit player’ and the Productivity Commission’s report ‘Business Set-up, Transfer and Closure’.[2]

The amendments to the AML/CTF Act in Part 2 of the Bill will apply AML/CTF regulation to businesses which exchange digital currencies for money. To achieve this policy reform, the Bill provides for a new definition of digital currency, creates a new designated service of exchanging digital currency for money and vice versa and establishes a new ‘Digital Currency Exchange Sector Register’ which is analogous to the existing Remittance Sector Register. Penalties will apply to persons who carry on a digital currency exchange business without first registering with AUSTRAC.

Most businesses in the digital currency exchange sector welcome the introduction of AML/CTF regulation, as they are already mindful of the risks posed by the services they provide. Many digital currency exchange providers also currently comply with an industry-based voluntary code of conduct that includes guidance on measures for protecting their services from illicit exploitation for money laundering and terrorism financing purposes. Industry representatives have advised that AML/CTF regulation of activities relating to convertible digital currencies will bolster public and consumer confidence in the sector.

---

[1] Established in 2006, Liberty Reserve was designed to avoid regulatory and law enforcement scrutiny and help criminals distribute, store, and launder the proceeds of credit card fraud, identity theft, investment fraud, computer hacking, narcotics trafficking, and child pornography by enabling them to conduct anonymous and untraceable financial transactions. It had its own digital currency, Liberty Dollars (LR), but at each end, transfers were denominated and stored in fiat currency.

[2] Refer to the Senate Economics References Committee inquiry into digital currencies (http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Digital_currency) and the Productivity Commission report on Business Set-up, Transfer and Closure (http://www.pc.gov.au/inquiries/completed/business/report/business.pdf).

Strengthening the investigation and enforcement powers of the Australian Transaction Reports and Analysis Centre (AUSTRAC)

Remittance sector reforms

The Bill implements a number of reforms to the operation of the Remittance Sector Register to strengthen the role of AUSTRAC as Australia's AML/CTF regulator. Remittance or money transfer businesses (remitters) are non-bank financial entities that transfer money on behalf of others. Remitters provide a relatively quick, low cost service, giving customers access to foreign regions and countries with limited or no financial infrastructure. The services provided by remitters are considered to pose a higher money laundering and terrorism financing risk than most other sectors and can often operate outside of the conventional banking system as they involve sending money to places that do not have established, modern banking networks.[3]

Cancelling registrations

Under section 75G of the AML/CTF Act, the AUSTRAC CEO currently has the power to cancel a remittance provider's registration if the registration involves, or may involve, a significant money laundering, terrorism financing or people smuggling risk, or if the person has breached one or more conditions of registration. However, the AUSTRAC CEO has no power to cancel a registered entity on the basis that it is inactive.

Recommendation 11.4 of the Report recommends that the AUSTRAC CEO be given stronger powers to control the registration of registered independent remittance dealers, registered remittance affiliates and registered remittance network providers (remittance providers) in order to assist in addressing some of the money laundering and terrorism financing risks posed by the remittance sector. Recommendation 11.4(a) provides that the AUSTRAC CEO should be allowed to deregister remittance providers that are not conducting remittance activities (as evidenced by a lack of reporting to AUSTRAC or other relevant activity).

Part 3 of the Bill amends section 75G to enable the AUSTRAC CEO to cancel the registration of a person if he or she has reasonable grounds to believe that the registered person no longer carries on a business that requires registration on the Remittance Sector Register. A power to deregister a remitter's registration once the remitter ceases to carry on a remittance business will ensure that the registration is not passed on to a third party and used to avoid scrutiny by AUSTRAC.

Renewing registrations

The power of the AUSTRAC CEO to renew registrations with conditions imposed is currently unclear. It is important for the AUSTRAC CEO to have this power to ensure the integrity of the Remittance Sector Register is maintained and remittance providers that have been found to be non-compliant can have conditions

[3] AUSTRAC, *Money laundering in Australia 2011*, 2011, www.austrac.gov.au.

imposed, where applicable, on the renewal of their registration. Accordingly, Part 3 of the Bill amends subsection 75E(1) to clarify that the AUSTRAC CEO has the power to renew registrations for remittance providers with conditions. The decision to renew a registration with conditions is reviewable in accordance with the provisions in Part 17A of the AML/CTF Act, including merits review in the Administrative Appeals Tribunal.

Part 3 also includes a minor amendment to section 75C of the AML/CTF Act, to expand the matters to which the AUSTRAC CEO should have regard when deciding whether to register a person who has applied for registration on the Remittance Sector Register. For the purposes of regulatory certainty, whether the registration involves or may involve a significant risk of facilitating 'other serious crimes' will now be a consideration the AUSTRAC CEO must take into account when determining whether to register a person on the Remittance Sector Register. This additional consideration – which has been replicated for the new Digital Currency Sector Register – will also ensure the integrity of the Remittance Sector Register is maintained and broaden the grounds on which the AUSTRAC CEO can decide to refuse a registration.

Issuing infringement notices

Currently, infringement notices can only be issued by the AUSTRAC CEO for a narrow range of offences listed under Part 15, Division 3 of the AML/CTF Act. For all other regulatory offences, the AUSTRAC CEO must apply for a civil penalty order through the Federal Court. This process is costly and time consuming and does not always allow AUSTRAC to respond in a timely and proportionate manner to secure reporting entity compliance.

Recommendation 15.4 of the Report recommends expanding the infringement notice provisions under subsection 184(1A) of the AML/CTF Act to include a wider range of offences established under the AML/CTF Act that are regulatory in nature. The Bill will implement this recommendation to give the AUSTRAC CEO more expedient and efficient means for promoting and encouraging compliance with these regulatory requirements.

The ability to issue infringement notices will only apply to a small number of civil penalty provisions, which include:

- subsection 32(1) (which deals with customer identification procedures to be carried out by reporting entities)
- subsection 41(2) (which deals with reporting certain suspicious matters)
- subsection 43(2) (which deals with reporting a threshold transaction)
- subsection 45(2) (which deals with reporting an international funds transfer instruction)
- subsection 47(2) (which deals with reporting on compliance with the AML/CTF Act and other instruments)

- subsection 49(2) (which deals with providing further information on request), and
- subsection 116(2), (3) or (4) (which deal with making and retaining certain records).

Safeguards are also built into the Bill to ensure that the AUSTRAC CEO cannot issue an infringement notice for trivial matters. The considerations which must be taken into account in a particular case include:

- the nature and extent of the contravention
- the seriousness of the contravention
- the circumstances in which the contravention took place, and
- any other matter the AUSTRAC CEO considers to be relevant.

AUSTRAC already has a record of considering the most appropriate mechanism to address non-compliance in each circumstance – ranging from working with the relevant entity to address any issues and prevent their recurrence, through to taking enforcement action. This measure will give AUSTRAC an additional tool to apply as appropriate.

Issuing remedial notices

Under section 191 of the AML/CTF Act, the AUSTRAC CEO currently has the ability to direct a reporting entity to take specified action to ensure the reporting entity does not commit any future breaches of their AML/CTF obligations. A civil penalty may apply for failing to comply with a remedial direction.

However, this power does not extend to a reporting entity's past obligations under the AML/CTF Act. This has particular implications where a reporting entity has failed to submit required transaction or suspicious matter reports to AUSTRAC. Currently, AUSTRAC must seek an enforceable undertaking or a court-ordered injunction to obtain this information.

Recommendation 15.3 of the Report recommends that the AML/CTF Act should be amended to expand the remedial directions power to allow AUSTRAC to direct reporting entities to remedy past contraventions of AML/CTF reporting obligations. Part 5 of the Bill will grant the AUSTRAC CEO the necessary power to require a reporting entity to rectify past non-compliance with the provisions of the AML/CTF Act. This power will be time-limited to conduct which occurred in the previous 24 months and will not apply to any activity which occurred prior to the commencement of the provisions of the Bill.

Providing regulatory relief to industry

The Report closely examined the operation of the existing AML/CTF regime and identified several areas in which regulatory relief could be provided to industry. Some key deregulatory measures have been included in the Bill.

Correspondent banking requirements

The Report concluded that the application of correspondent banking requirements under the AML/CTF Act to *nostro* and *vostro* accounts is unclear and out-of-step with international banking standards and practices.

A *nostro* account is an account that an Australian financial institution holds with a foreign financial institution to facilitate transactions on behalf of the Australian financial institution's customers. A *vostro* account is an account that a foreign financial institution holds with an Australian financial institution in order to facilitate transactions on behalf of the foreign financial institution's customers. International practice is that AML/CTF measures should only apply to *vostro* accounts as this is where the associated money laundering or terrorism financing risks lies. However, the current lack of clarity means that some regulated businesses unnecessarily apply AML/CTF measures to both types of accounts. Accordingly, the Bill clarifies that customer due diligence need only be conducted in relation to *vostro* accounts.

The Bill also makes a change to the arrangements regulating correspondent banking relationships. The Report noted that the definition of correspondent banking under the AML/CTF Act is unduly narrow and fails to capture some banking relationships that are recognised as correspondent banking relationships under international banking practice. This narrow definition of 'financial institution' means that Australian banks are operating at a competitive disadvantage by having to apply more stringent customer due diligence measures to certain banking relationships compared with their international counterparts. The Bill will remedy this competitive disadvantage by providing the AUSTRAC CEO with the power to expand the definition of 'financial institution' for the purposes of specific provisions of the AML/CTF Act. It is intended that the AUSTRAC CEO will exercise this power specifically in relation to the requirement to conduct customer due diligence on correspondent financial institutions in Part 8 of the AML/CTF Act. Given the diversity of practice internationally in relation to the definition of 'financial institution', AUSTRAC may need to use this rule-making power flexibly and will be able to choose to prescribe either individual entities or classes of entities as financial institutions for the purposes of the correspondent banking provisions in Part 8.

Deregulating insurance intermediaries and general insurance providers under the FTR Act

The AML/CTF Act operates alongside the FTR Act. The FTR Act was introduced in 1988 to assist in administering and enforcing taxation laws as well as other Commonwealth, State and Territory legislation. With the introduction of the AML/CTF Act in 2006, certain parts of the FTR Act were repealed or became inoperative but the FTR Act continues to impose some regulatory requirements for 'cash dealers' and solicitors. A cash dealer must submit significant cash transaction reports (SCTRs) and suspect transaction reports (SUSTRs) to AUSTRAC, while solicitors must report SCTRs.

The definition of a cash dealer under the FTR Act currently includes:

- insurance intermediaries, such as motor vehicle dealers and travel agents, and
- general insurance providers, such as motor vehicle dealers.

The FATF's international standards for combating money laundering and terrorism financing only require life insurance and investment-related insurance products to be regulated and not general insurance. Services provided by travel agents acting as insurance intermediaries pose a low money laundering and terrorism financing risk, as do general insurance providers (other than motor vehicle dealers). In view of this, the Bill will deregulate these service providers.

Deregulating the cash-in-transit sector

Cash-in-transit (CIT) operators are currently subject to AML/CTF compliance and reporting obligations because they provide designated services associated with the secure collection and delivery of physical currency.

The AML/CTF regulation of CIT operators in Australia predates the founding of the FATF. CIT operators were first subjected to regulatory obligations under the *Cash Transactions Reports Act 1988* as 'cash dealers' on the basis that they collect and deliver currency. CIT operators continued to be subjected to AML/CTF regulation under the FTR Act and more recently under the AML/CTF Act.

The Report concluded that there are low or negligible inherent money laundering and terrorism financing risks associated with the domestic transportation of cash from one place to another by a contractor such as a CIT operator. Securely moving cash using a licensed third party operator within Australia is not, in itself, a money laundering typology and the FATF standards do not require countries to apply AML/CTF regulation to CIT operators. The physical movement of cash internationally across borders is, however, an established money laundering typology and the risks associated with such movements of cash are monitored as part of the cross-border reporting regime under the AML/CTF Act.

In light of the assessment of low risk, the Bill will repeal the designated services in the AML/CTF Act which apply to CIT operators and amend the definition of cash dealer in the FTR Act to exclude CIT operators. The removal of the AML/CTF obligations should produce regulatory efficiencies because CIT operators and their staff are separately subject to licensing obligations by the States and Territories.

Improving the utility of the 'designated business group' concept

Some businesses or persons regulated under the AML/CTF regime have a commercial association through ownership that enables them to join together as a 'designated business group' (DBG) and share certain obligations under the AML/CTF Act. This can assist these businesses to minimise the burden of complying with regulation across the group. The AML/CTF Act recognises DBGs as an exception to the prohibition on 'tipping off' in Part 11 (Secrecy and Access), which prohibits persons making suspicious matter reports from disclosing that they have made such a report to anyone other than AUSTRAC.

The current definition of a DBG under the AML/CTF Act does not necessarily align with how businesses actually structure themselves. In particular, a DBG is not the same concept as a 'corporate group' as set out in the *Corporations Act 2001*. This can lead to the duplicate reporting of suspicious matters as two entities within the same corporate group, but not the same DBG, must lodge suspicious matter reports. A particular concern is that related bodies corporate are currently unable to share information about joint customers, thereby impeding the ability to effectively and efficiently manage the money laundering and terrorism financing risk associated with a joint customer across the corporate group.

The Bill will amend Part 11 of the AML/CTF Act to allow reporting entities to share information within their corporate group, as defined under the *Corporations Act 2001*, in addition to within a DBG. It does not modify the concept of a DBG as the concept still has relevant application to reporting entities that are not corporations.

Qualifying the term 'in the course of carrying on a business'

During the statutory review, industry stakeholders noted an inconsistency in the operation of the designated services in the AML/CTF Act. A number of the designated services in table 1 of section 6 (related to financial services) only capture activity carried out 'in the course of carrying on a business' specifically related to that service. For example, item 10 of Table 1 captures supplying goods by way of lease under a finance lease, but only where this service is provided in the course of carrying on a finance leasing business.

However, the designated services in Table 2 (bullion dealing) and Table 3 (gambling services) of section 6 do not contain such a caveat. For example, the buying and selling of bullion is captured under items 1 and 2 of Table 2, where the buying and selling is conducted in the course of carrying on any business. 'Business' is very broadly defined under the Act as a 'venture or concern in trade or commerce, whether or not conducted on a regular, repetitive or continuous basis'.[4]

This means that entities which only provide these services very occasionally or as incidental to their core business are potentially captured under Australia's AML/CTF regime and subject to the costs of complying with Australia's AML/CTF regime. For example, a pub that only facilitates gambling (e.g. "Two-up") on ANZAC day.

[4] Section 5 of the AML/CTF Act.

The amendments to Part 4 will rectify this inconsistency and ensure that Table 2 and Table 3 of section 6 are consistent with the Replacement Explanatory Memorandum to the AML/CTF Act which states:

> as a general proposition, designated services are limited to services provided to a customer in the course of carrying on the core activity of a business and do not capture activities which are peripheral to the core activity of the business [...] Some businesses may have more than one core activity and whether an activity is a core activity of the businesses will be determined by the circumstances of each case.[5]

It is not anticipated that this change will affect a significant number of entities. For instance, there is often an overlap between entities which provide designated services under Table 1 and Table 3 of section 6. The addition of caveats in the gambling designated services will mean that entities which do not provide these services in the course of carrying on a gambling business will still be captured by Table 1 and regulated under Australia's AML/CTF regime.

Broadening the powers of police and customs officers at the border

The Report considered that Australia's existing cross-border reporting regime limits the ability of police and customs officers to adequately search and seize physical currency and bearer negotiable instruments (travellers' cheques, money orders etc.) at the border. Instead, the search and seizure powers under the AML/CTF Act are linked to breaches of the current cross-border reporting requirements, which require travellers to declare physical currency of $10,000 or more and declare, on being questioned, if they are carrying a bearer negotiable instrument.

This leaves gaps in the ability of police and customs officers to search and seize physical currency and bearer negotiable instruments where officers have a suspicion that funds or instruments may be linked to money laundering, terrorism financing or other serious crimes, but the person has not breached the reporting requirements in the AML/CTF Act. The Bill will strengthen the ability of police and customs officers to enforce these reporting obligations by establishing search and seize powers for cash, travellers' cheques and other items.

In addition, only criminal penalties are currently available for the cross-borders offences established under the AML/CTF Act. Given the higher burden of proof required for prosecuting criminal offences, this limits the utility of these provisions for authorities. In order to provide more expedient and efficient means for pursuing compliance with the AML/CTF Act, the Bill will allow authorities to pursue civil penalties for this conduct.

---

[5] Sub-clause 6(2), *Anti-Money Laundering and Counter-Terrorism Financing Bill 2006 Replacement Explanatory Memorandum*, http://www.comlaw.gov.au/Details/C2006B00175/Other/Text.

Conclusion

Overall, the Bill will enact important reforms to strengthen and streamline Australia's AML/CTF regime. The measures have been developed in accordance with the recommendations of the Report and have been the subject of extensive consultation with industry and key Commonwealth agencies.