Australian Banking Association

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Director
Transnational Crime Policy Branch
Law Enforcement Policy Division
Department of Home Affairs
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Proposal to legislate and reform Chapter 75 Exemptions

The Australian Banking Association (**ABA**) welcomes the opportunity to provide comment on the Department of Home Affairs' consultation, along with the Australian Transaction Reports and Analysis Centre (**AUSTRAC**), on a proposal to legislate and reform Chapter 75 of the *Anti-Money Laundering and Counter-Terrorism Financing Rules 2007* (AML/CTF Rules).

Our position

The ABA supports opportunities for better information sharing between Reporting Entities (REs) and law enforcement where it leads to better community outcomes and reduces the threat of criminals using the financial system to commit crimes. In principle, reforms to the Chapter 75 exemption could create closer linkages with law enforcement to assist with this aim. However, the ABA does not consider that the proposed reforms will achieve the stated outcomes of streamlining processes, reducing administrative burdens for government or industry or driving greater compliance.

On the contrary, we submit these changes would:

- **Result in a significant regulatory burden and cost for both industry and law enforcement agencies (LEAs)**. This proposal shifts the administration that is currently undertaken by a single regulator to multiple Reporting Entities (REs). REs will need to duplicate administration and outreach to multiple LEAs, create or retrain teams and modify systems to assess and process Chapter 75 requests. REs will also need to adapt compliance and assurance regimes to ensure notices are within the law given the REs would assess notices.

  Further, the additional proposed requirement such as the need to file suspicious matter reports (SMRs) when relying on a notice appears to add an additional layer of operational burden on REs without necessarily improving the intelligence value of those SMRs.

- **A likely surge in the number of Chapter 75 requests**. We anticipate the ease of issuing a notice will see a spike in the receipt of these exemption requests. This will necessitate additional resourcing and divert resources from actioning requests to assessing them to ensure compliance with regulatory requirements. As a result, some REs that currently apply 'good faith' processes such as embargoes to prevent the exit of customers may decide to discontinue these processes to ensure it complies with the proposed obligations.

- **Create legal uncertainties on regulatory obligations for REs**. Removing AUSTRAC from this process introduces an additional risk as the onus is on REs to assess the legality of the notices. REs could be subject to future enforcement action should the regulator deem that the RE was non-compliant in accepting or rejecting a notice. As a result, REs will likely take a 'compliance first' approach, resulting in more scrutiny of notices and less flexibility in actioning requests to reduce risks of non-compliance. This is also likely to affect some banks' application of processes such as embargoes on customer exits.

- **Introduce inconsistencies in the application of notices**. LEAs and REs will apply their judgments based on their own frameworks when accepting or refusing a notice. This will result in multiple standards and create inconsistent outcomes. This in turn creates risks and will tend to make REs apply very conservative thresholds so they do not fall foul of the law.

- **Reduce the quality of Chapter 75 processes**. With the potential increase in Chapter 75 notices, and the diversion of resources to assessing the validity of the notice, REs will no longer be able to provide the level of engagement currently provided and this will reduce the overall quality of the process.

  We also note that LEAs may be more comfortable providing sensitive details of an investigation to AUSTRAC than to an RE. As a result, REs may not receive enough information to adequately assess or action requests particularly if they are of a sensitive nature.

  Finally, situations of poor coordination or duplication might also arise where different LEAs could submit Chapter 75 notices to REs without knowing that others have also done so. In the current process with AUSTRAC being the coordination point these potential situations of duplication could be de-conflicted at an early point.

Key recommendations

The ABA recommends not proceeding with this proposal until the issues identified above are considered and resolved and further industry consultation is undertaken. If implemented, the ABA recommends that the legislation and regulations establishing this framework:

1. **Ensures an effective governance and oversight framework.** A governance and oversight framework is necessary to ensure Chapter 75 requests are made within the statutory requirements with appropriate guidance to LEAs and sufficient protections for REs in actioning requests. AUSTRAC should have oversight of all notices and provide a forum for LEAs and REs to query and seek clarification over whether a particular notice complies with the law and regulations. The ability for LEAs and REs to check with AUSTRAC would be invaluable and ensure more consistent outcomes.
2. **Retains the ability for REs to refuse to accept notices.** Consistent with the current approach to Chapter 75 requests, REs should be able to refuse to action notices where they pose an excessive legal or compliance risk, do not meet the statutory requirements, or are too late because the customer has been exited or enhanced customer due diligence (ECDD) processes are in place may tip off the customer.
3. **Provides effective protections to REs where actions are taken to execute a notice.** A strong role for AUSTRAC in this process currently affords REs comfort when executing a notice. With the removal of AUSTRAC from the process, REs require stronger defences to ensure their actions in line with a notice are not subject to later enforcement action. REs should be assured their determination that exemptions can lawfully apply will be given the presumption of being correct and if a regulator wishes to challenge their decisions in the future, the onus should be on them to prove that REs have breached clauses in the Act.
4. **Requires law enforcement consultation with REs before lodging a Chapter 75 request.** The current framing allowing a valid notice without consultation is inadequate and exposes REs to a range of legal and compliance risks. Compulsory and early consultation will ensure that compliance processes are not already being applied and steps are not already being taken to exit a customer.
5. **Sets clear expectations on REs**. Accompanying this legislation should be clear rules and guidance from AUSTRAC that assists REs in meeting notice obligations, including evaluating the merits of the notices and provides appropriate protections (such as in relation to the scope of a notice).
6. **Provides adequate lead time for changes.** REs will need to establish processes, train (and add) staff and update systems to assess and administer the likely influx of requests. REs will also need to strengthen legal teams to ensure the requests are consistent with their broader obligations under AML/CTF and other legislation such as sanctions and proceeds of crime.
7. **Retains REs discretion on when to submit an SMR.** As it is not always appropriate or necessary to submit an SMR, and would significantly add to the regulatory burden, REs should

only be required to submit an SMR where it forms a suspicion for the purpose of s 41 of the AML/CTF Act.

Consultation process

The ABA notes that this consultation process has not provided industry with a sufficient opportunity to understand or adequately engage with the details of the proposal.

The consultation paper does not provide details of governance and compliance matters and provides little detail on how regulator oversight would occur. The paper also does not provide analysis of the regulatory cost on industry or consider whether the benefits outweigh the costs.

Further, we are concerned that industry will not see or be able to comment on an exposure draft of the legislation, which is unacceptable given the significance of the proposed change.

Finally, not all affected REs are being consulted, particularly members of the Customer Owned Banking Association (COBA), whose members are likely to be disproportionately affected along with smaller ADIs that are ABA members. We consider that a consultation should be undertaken on all affected REs which is broader than the members of the ABA and AFMA.

The following pages provide additional information and answers to the questions.

Thank you for the opportunity to provide feedback. If you have any queries, please contact me at Prashant.ramkumar@ausbanking.org.au

Yours sincerely,

Prashant Ramkumar
Associate Policy Director

Australian Banking Association

Responses to consultation questions

1. **What challenges do you currently face when receiving/complying with a Chapter 75 notice?**

As a general comment, the ABA considers the current regime is working reasonably well and we do not consider substantial change is required. There are certainly areas for improvement, for example:

- Notices often do not extend to associated individuals and/or businesses. If due diligence was performed and those parties exited, the persons of interest may infer they are under investigation.
- LEAs often are not aware that the notice is about to expire and requires proactive action from REs to notify them. This places REs at some risk on occasions where LEAs ask to keep the exemption in place even though the notice has expired or where they say they are in the process of extending it.
- LEAs issuing a notice too late (i.e., where a customer is being exited), providing wrong information on the customer and a lack of information provided on the investigation or the progress of the investigation making it harder for REs to determine the risks posed by a customer and their own exposure to compliance risks.

Further, under the current regime REs often have a lack of context from AUSTRAC regarding the reasons for issuing a notice and those notices are sometimes not sent to the right recipients within the RE, resulting in delays on occasions. Further, notices sometimes occur on individuals upon whom ECDD process are underway which increases the risk of the person of interest exiting or inferring they are under investigation.

We consider all these as improvements to ensure better communication between AUSTRAC, LEAs and REs, but these should be considered as tweaks to the existing regime rather than requiring a new framework.

2. **Do you have any concerns/comments on the proposed reforms outlined above or foresee challenges? If so, do you have ideas on how they could be overcome?**

Yes, as discussed in our position above.

3. **In relation to the requirement for consultation at Paragraph 17, the intent is to reflect this in the AML/CTF Act. However, given a failure to consult would not invalidate the notice, the Department is currently considering whether this requirement could be included in the AML/CTF Rules. Do you have any views on this?**

See Recommendation 4 above. We believe the requirement to consult is essential and are concerned with the idea that LEAs will be able to provide a notice without consultation.

Where an LEA chooses to provide a notice without consultation, this could expose REs to legal and compliance risks where the notice is not consistent with legal and compliance obligations (such as whether the notice relates to a serious offence).

In addition, early consultation is essential should notices be effective. In instances, customers may be exited or be subject to ECDD and that would make the notice less effective as the customer may infer that they are under investigation. Furthermore, given the incidents of wrong details of an individual which take time for REs to correct before processing an application, it is prudent for LEAs to consult early to ensure the right customer is identified early and the process is started quickly once the notice is in effect.

In terms of whether this should be in primary legislation, we consider a consultation requirement be in the Act with further requirements in terms of timing and other matters be further specified in the rules.

4. **In relation to the requirement for consultation, do you have any suggestions on how the Department can best strike the balance between early and effective consultation, the administrative burden on eligible agencies, and mitigating risks associated with the impact of a notice (such as de-banking)?**

As noted above, early consultation will reduce the potential risk that a customer is exited (based on high ML/TF risk) and ensure REs can quickly and effectively assist LEAs. The regulatory burden would be reduced the extent to which LEAs can clearly articulate their requirements so there is minimal follow up required from REs. An early conversation followed up by compliant and clear documentation will assist in this process.

More broadly, the ABA considers that clear regulatory expectations are required, with safe harbours for REs in actioning those requests. This will ensure REs have the comfort that they can action requests without taking an excessively compliance centred approach that can add to the regulatory burden for LEAs.

We suggest that AUSTRAC should also play a role in ensuring that the principles of Chapter 75 are not departed from in practice by LEAs, and that associated processes do not become overly onerous.

5. **In relation to the exemption period, the intent is to remove the existing six-month default exemption period in the Rules and replace it with a more flexible mechanism that would better reflect the tailored approach we want to facilitate (and better aligns with the risk-based approach that sits at the centre of the regime). We also want to ensure that, after the appropriate exemption period, the power to issue further notices returns to AUSTRAC. This will ensure that the exemption will not continue in perpetuity. Do you have any suggestions on how best to give effect to this?**

The ABA broadly supports some flexibility in the exemption period and for AUSTRAC to issue further notices. However, we do consider that the initial exemption period should be limited to the time that is necessary and without a clear timeframe. Without this, REs may be exposed to risks around customer exits, enhanced customer due diligence, and tipping off.

There should be a requirement to explain the reason for a longer period for the exemption to remain in place (i.e., more than 6 months). This is important as without a clear guardrail we could see exemptions applied as a default for longer periods than required. One possible solution is that any notice seeking an exemption period of more than 6 months require AUSRAC CEO approval.

Finally, the proposal for AUSTRAC to issue further notices is generally supported, but it is not clear how this will apply in practice unless AUSTRAC has visibility over all exemption notices to be able to make sufficiently informed decisions. Without this visibility, we question to what extent AUSTRAC will be able to make that informed decision and may result in simply a 'rubber stamping' approach. Furthermore, if an RE finds new information that makes them uncomfortable in retaining the customer, the RE should be able refuse an extension request even if made by AUSTRAC.

6. **What would you like to see included in guidance to support reporting entities to comply with the proposed reforms?**

The guidance should clearly outline what REs are expected to do in actioning those notices while meeting broader statutory obligations, including circumstances where an RE can reject the notice. Examples should be provided on where ECDD can and should be performed should also be guided, including examples where it should not be done.

The guidance should set out AUSTRAC's expectations around informal requests to not take action on accounts from LEAs and what AUSTRAC expects REs to do when notices expire (even if LEAs are requesting that we continue to operate under the notice).

The guidance should explain the breadth of relief granted by a notice and also guide REs on circumstances where they can contact AUSTRAC or any other party to inform them of any matter relating to a notice. Current wording relates to informing the AUSTRAC CEO of anything that impacts the notice.

Further guidance is required on the issue of customer exits and the circumstances and protections in place for REs since Chapter 75 requests are being relied upon to defer exits. This consultation does not provide sufficient information in relation to this issue.

In relation to the submission of an SMR, further guidance is needed on whether REs should disclose whether a Chapter 75 notice is in place. Current practice is to not disclose a notice is in operation due to the covert nature of these operations. We would advise AUSTRAC to consult with LEAs if they agree with this approach and we would seek clarification on this point in AUSTRAC's guidance.