

24 October 2014

Consultation Paper No. 2 – AUSTRAC Industry Contribution
Legal and Policy Branch
AUSTRAC

By Email Only: Policy_Consultation@austrac.gov.au

FSC Submission on AUSTRAC Industry Contribution – Second Round Consultation

The Financial Services Council (**FSC**) represents Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advisory networks, trustee companies and public trustees. The FSC has over 125 members who are responsible for investing more than \$2.2 trillion on behalf of 11 million Australians.

We welcome the opportunity to comment on the *AUSTRAC Industry Contribution: Second stakeholder consultation discussion paper* (the **Second Discussion Paper**), released for consultation on 25 September 2014. We value our relationship with AUSTRAC and acknowledge AUSTRAC is open, communicative and consultative and has made itself available to FSC and FSC members in relation to this consultation (as well as other AUSTRAC consultations).

1. This submission *firstly* sets our comments, in response to the Second Discussion Paper, on the design of the Industry Contribution and requests refinements to improve the efficiency and equity of the operation of the Industry Contribution. We also enquire about the basis of the exemption of the Industry Contribution (more particularly the draft *AUSTRAC Industry Contribution Determination 2014 (No. 1)*) from a Regulatory Impact Statement (**RIS**) as the basis of the RIS exemption is not apparent from the consultation material (which only notes that the RIS exemption has been granted without setting out the basis and reasons for the RIS exemption).
2. *Secondly*, this submission reiterates our comments made in our 24 July 2014 submission on the *AUSTRAC Industry Contribution discussion paper* (the **First Discussion Paper**), released for consultation on 26 June 2014. While such matters are a Government policy matter, we wish to reiterate our concerns with the AUSTRAC Industry Contribution model as it applies to AUSTRAC, the beneficiaries of AUSTRAC regulation, AUSTRAC financial intelligence functions and Australia's AML-CTF regime. The Industry Contribution results in leviable reporting entities funding non-regulatory activities of AUSTRAC (the financial intelligence function). Further, by levying 100% (by 2017-2018) of AUSTRAC's funding on leviable reporting entities, this imposes all the AUSTRAC costs on only a sub-set of the beneficiaries of AUSTRAC regulation.

3. *Thirdly* we make some brief comments – intended to be constructive - reflective of concerns of our members, about the number of concurrent AML/AUSTRAC related consultations, which thereby impacts the ability of consultations to be considered comprehensibly by industry.

Comments on AUSTRAC Industry Contribution: Second stakeholder consultation discussion paper (the Second Discussion Paper)

4. There does not appear to have been any significant changes between the proposals between the First Discussion Paper and the Second Discussion Paper.

Treatment with respect to the ‘earnings component’ of the proposed Industry Contribution model

5. Many reporting entities will derive operational income from both direct earnings (related to the *designated services* they provide) and also indirect earnings from subsidiary entities which have *no connection to the provision of designated services*. In these situations consolidated income from these subsidiaries or earnings derived from dividends from subsidiaries does not fairly represent the operational activity related to *designated services* regulated under AML/CTF legislation.
6. The current proposals in the Second Discussion Paper does not contemplate these circumstances and we would like to clarify treatment of the calculation of the Industry Contribution. FSC requests that AUSTRAC’s Industry Contribution be limited (calculated on) to the direct earnings of the given reporting entities. Should an entity have a subsidiary that also offers *designated services* it would also be levied separately in its own right.
7. FSC understands that the earnings component of the Industry Contribution should take account of the need to achieve a ‘simple’ and ‘externally verifiable’ earnings component. FSC submits that a contribution based on a reporting entity’s ‘unconsolidated earnings’ (as opposed to ‘consolidated earnings’ in the current proposal) meets both these objectives. Unconsolidated earnings are simple for a reporting entity to obtain/provide and are also externally verifiable.
8. Should this distinction not be applied and reporting entities (or DBGs) are levied based on income derived from all sources/activities (i.e. in addition to those related to the provision of *designated services*) the allocation of costs (that is the Industry Contribution) may be disproportionate and unreasonably impact specific industry participants depending on the nature of any activities of subsidiaries (not undertaking designated services).
9. We acknowledge that ultimately AUSTRAC needs to recover what it needs to recover based on a Government appropriation (i.e. the size of the “pie” to be collected is set by Government as an appropriation). The above comments are not inconsistent with that principle. Our comments above go to the equity of the division of the Industry Contribution (or the division of the “pie”) – this assumes that none of the “pie” is to be collected via Government consolidated revenue, in which case we reiterate our submission on the First Discussion Paper (and as summarised in paragraphs 19 to 24 of this submission.)

Treatment of foreign earnings – foreign entities are only assessed on Australian earnings whereas Australian entities are assessed on worldwide earnings

10. In the draft *AUSTRAC Industry Contribution Determination 2014 (No 1)* the total profit or total earnings of a leviable entity that is a foreign company or subsidiary of a foreign company is a reference to the total profit or total earnings of the leviable entity *which are derived from operations in Australia*. Whereas we understand that under the draft *AUSTRAC Industry Contribution Determination 2014 (No 1)*, earnings of Australian based leviable entities are not limited to earnings derived from operations in Australia – we think for equity they should be also limited to earnings derived from operations in Australia, particularly given earnings is not currently limited by reference to earnings from *designated service* activities (see our comments in paragraphs 5 to 9 inclusive on that point).

Budgeting process for reporting entities – easing the administrative burden on levied reporting entities on collecting the Industry Contribution – Issue one invoice each year

11. Under the proposals the Government may determine one or more appropriations to be collected by AUSTRAC under the Industry Contribution. The current proposal contemplates that it may be necessary to seek multiple industry contributions within a single year.
12. Reporting entities need to undertake a budgeting process which sets the reporting entity's budget prior to the commencement of the relevant financial year. Budgets are set by management and boards and are an important accountability mechanism for shareholders (of reporting entities) who should know in advance of the relevant financial year the likely expenses of a reporting entity in *the next* financial year. We request that where more than one appropriation for AUSTRAC is made by the Government in a single year, that the second and subsequent appropriations be "rolled up"/"carried over" to the Industry Contribution invoice for the next following financial year *so that reporting entities only receive and pay one Industry Contribution invoice per year*. Multiple invoices, intra-year, provide difficulties with budget approval processes. If AUSTRAC only issue one Industry Contribution invoice per year, AUSTRAC will still be able to collect the amount the subject of appropriations (by adding to the next year any second or subsequent appropriation from a prior year).

Providing Notice of contribution amount

13. The contribution amount to be paid by levied reporting entities is a function of earnings of leviable reporting entities and the Government appropriation for AUSTRAC. We request that as much prior notice as possible be given to reporting entities as to the earnings component and transaction reporting component percentages. This is necessary for budget and planning purposes of reporting entities.

A tiered application of the earnings component of the industry Contribution

14. Having a single defined threshold for the earnings requirement creates inequitable scenarios. Entities with very similar earnings that are either side of the \$100 million earnings threshold

(for the earnings component of the Industry Contribution) face dramatically different contributions despite their similar capacity (assuming all income in each case is derived from *designated service* type activities).

15. An entity that receives earnings of more than \$100 million only in certain years may find itself faced with dramatically different AUSTRAC expenses from one year to the next. A scaled series of thresholds (instead of the single \$100 million threshold) would be a more equitable approach.

Basis of exemption from Regulatory Impact Assessment

16. The *AUSTRAC Industry Contribution: Second stakeholder consultation paper* states on page 8 appearing under *Attachment 2: Draft explanatory statement to the Ministerial Determination* under the heading “Regulatory Impact Statement”:

“An exemption has been granted from the requirement to make a regulatory impact statement”.

17. Given the significant additional fiscal regulatory burden that the Industry Contribution imposes on leviable reporting entities, we request that AUSTRAC provides information as to the basis upon which the RIS exemption was applied for and provided, and which of the available RIS exemptions formed the basis of the RIS exemption which has been granted for the Industry Contribution. We consider this important as a matter for transparency, and for future regulatory proposals. We make this request as the only statement we could locate on the RIS exemption for the Industry Contribution was a statement (quoted in paragraph 16 above) that an RIS exemption has been granted. It may be that the RIS exemption was provided by Government under the process for RIS exemptions, however information on the basis of the exemption from an RIS is not contained in any of the consultation material as part of the *AUSTRAC Industry Contribution: Second stakeholder consultation*.
18. We request AUSTRAC inform and make available to reporting entities, the basis of the granted RIS exemption and the basis upon which any application for an RIS exemption was made.

AUSTRAC Industry Contribution discussion paper (the First Discussion Paper) – issued June 2014 – we reiterate our comments on the benefit of AUSTRAC regulation for other stakeholders who bear none of the costs of AUSTRAC

19. We refer to and we reiterate all our comments in our 24 July 2014 submission on the *AUSTRAC Industry Contribution discussion paper (the First Discussion Paper)*, released for consultation on 26 June 2014.
20. As set out in our 24 July 2014 submission to the First Discussion Paper, we note that (by 2017-18) leviable reporting entities are to fund *all* of AUSTRAC’s operational expenditure (including an allowance for depreciation and including AUSTRAC’s non-regulatory functions namely financial intelligence functions), yet the Australian Taxation Office and Australian crime and

policing authorities and agencies, the Australian community generally, Australian taxpayers, the Australian Government, and the business community broadly (which dwarfs the leviable reporting entities) also share in the benefit of regulation by AUSTRAC and Australia's laws relating to anti-money laundering. It is in our view obviously *not* the case that the *only* and *sole* beneficiaries of AUSTRAC regulation and AML laws are those leviable reporting entities to be invoiced the Industry Contribution. A 100% contribution by leviable reporting entities with no commensurate contribution via Government consolidated revenue is not consistent, in an equity sense, with a regime which benefits (as well as levied reporting entities) non-levied reporting entities, non-reporting entities, ATO, enforcement authorities and the other beneficiaries above. To the extent that instead the matter is driven by a Government policy decision to assist in the Budget repair, rather than a decision as to how to allocate funding of AUSTRAC to *all* beneficiaries of AUSTRAC regulation (which would need a combination of AUSTRAC levies and funding via Government consolidated revenue), then that is a policy matter for Government. *In our view, there is a strong case in particular for a commensurate (and pre-dominant) contribution of the financial intelligence function of AUSTRAC out of Government consolidated revenue.*

21. By 2017-18 the Industry Contribution will recover 100% of AUSTRAC's budgeted operating expenditure (including depreciation). To the extent that the amount and extent of the (100%) Industry Contribution is based on an argument (set out by AUSTRAC in the First Discussion Paper) that industry obtains a benefit by being regulated by AUSTRAC, *we note that there are many other beneficiaries of AUSTRAC regulation* in addition to the benefits to leviable reporting entities set out on page 5 of the First Discussion Paper. Other beneficiaries of AUSTRAC regulation include:
- (a) The Australian Taxation Office and Australian taxpayers (we note that AUSTRAC regulation assists in ascertaining potential tax avoidance, and the ATO has had significant success in this regard);
 - (b) the Australian Government, in terms of international liaison and credibility at international bodies (such as FATF);
 - (c) the business community broadly (including entities which are not reporting entities under the AML regime); and
 - (d) Australian crime and policing authorities and agencies, who benefit from the financial intelligence function of AUSTRAC particularly.
22. Superannuation trustees and investment managers (who are agents for superannuation funds and other collective investment schemes) do not represent a significant AML risk to support/justify a significant increase in the contribution to funding AUSTRAC. Many of these entities will incur a significantly increased contribution under the Industry Contribution proposals. There is not an increase in AML risk in this sector (for example) to support an increased funding to AUSTRAC (this is aside from the fact that there is under the Industry Contribution proposal many other (non-contributing) beneficiaries of AUSTRAC regulation and Australia's AML laws – see above).

23. We also observe that other areas of potential AML-CTF regulation and sources of AML-CTF risk, namely Tranche II of the AML reforms, are not currently captured by the AML-CTF regime and (necessarily) are not contributing to the Industry Contribution even though they also may be a source of AML-CTF risk. This should be considered by the Government (including refining the Industry Contribution if and once Tranche II are covered by the AML-CTF regime).
24. We think it is very difficult to argue that the primary or sole or pre-dominant beneficiaries of the financial intelligence function (which is to be funded by leviable reporting entities under the Industry Contribution model) are leviable reporting entities rather than criminal law enforcement agencies and the Australian Taxation Office. *That is, in our view, there is a strong case in particular for a commensurate (and pre-dominant) contribution of the financial intelligence function of AUSTRAC out of Government consolidated revenue.* This is not to suggest that it is only criminal enforcement agencies and the Australian Taxation Office which benefit from financial intelligence in a broad sense; as others benefit including (collectively) the (non-levied) groups mentioned in paragraphs 20 to 21 above as well as leviable and non-leviable reporting entities. However, leviable reporting entities are to fund 100% of AUSTRAC's functions, including the financial intelligence functions. *This is not an equitable contribution arrangement and we urge re-consideration of the inequity of the current design of the proposed Industry Contribution model.*

Concurrent and multiple AML/AUSTRAC related consultations – Industry feedback

25. We have some general comments in relation to the number of concurrent AML/AUSTRAC related consultations which FSC members have expressed concerns to FSC about. FSC considers AUSTRAC ought to be made aware of this and hence we make some general comments on the number of consultations which is straining the ability of FSC members and other reporting entities to provide a comprehensive and considered response to some AUSTRAC led consultations.
26. FSC very much welcomes consultation which is essential. FSC also applauds AUSTRAC's consultation process and notes that AUSTRAC provides open and accessible consultation, reaches out to FSC and FSC members on AUSTRAC related consultations as well as hosting the AUSTRAC Financial Industry Consultative Forum. This is welcomed and should continue.
27. As an observation and intended as a constructive comment, there are a number of AML related consultations being conducted concurrently, including the Industry Contribution and the Compliance Report consultation (the later needing in particular a very detailed review and consideration by reporting entities). This is in addition to the AML Act Review (ongoing) which may in future involve consultation.
28. Any ability to stagger consultations, where appropriate and feasible, would improve the comprehensibility of industry responses to consultations. We acknowledge sometimes this is not feasible due to Government or FATF timing commitments but we request that the staggering of consultations be considered where that is feasible. We reiterate that our

comments are limited to the number of concurrent consultations and is no way a criticism of the manner and comprehensiveness of AUSTRAC led consultations.

If you have any questions on our submission, please contact Stephen Judge on (02) 9299 3022.

Yours sincerely

A handwritten signature in blue ink that reads "Stephen Judge". The signature is written in a cursive style with a large initial 'S' and 'J'.

STEPHEN JUDGE
General Counsel