Australian Privacy Foundation

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Changes to AMF/CTF Rules relating to customer due diligence (CDD)

Response to draft rules issued for comment in December 2013

Submission to AUSTRAC

January 2014

The Australian Privacy Foundation

The Australian Privacy Foundation is the main non-governmental organisation dedicated to protecting the privacy rights of Australians. The Foundation aims to focus public attention on emerging issues which pose a threat to the freedom and privacy of Australians. Since 1987, the Foundation has led the defence of the right of individuals to control their personal information and to be free of excessive intrusions. The Foundation uses the Australian Privacy Charter as a benchmark against which laws, regulations and privacy invasive initiatives can be assessed. For further information about the Foundation and the Charter, see www.privacy.org.au

Please note that APF does not have a single postal address – we prefer communication by e-mail. If a postal address is required please contact the signatory.

Publication of submissions

We have no objection to the publication of this submission in full. To further the public interest in transparency of public policy processes, APF strongly supports the position that all submissions to public Inquiries and reviews should be publicly available, except to the extent that a submitter has reasonable grounds for confidentiality for all, or preferably part of, a submission.

Introduction and general comments on the AML/CTF regime

Our concerns and comments relate to the CDD requirements in respect of individual customers (i.e. natural persons) who have privacy rights under Australian law. We make no comment in relation to CDD requirements in respect of legal entities, since we accept that legal entities do not have privacy rights, and that the privileges conferred by corporate, trust, association or cooperative status justify a higher level of intrusion by the state into their affairs, compared to individual natural persons.[1] That is not to say that individuals who are owners or directors of companies, trustees, or officers of associations or cooperatives may not have legitimate concerns about the level of intrusion involved in the CDD requirements relating to legal entities.

[1] The situation of partnerships is complex as we understand that they are not separate legal entities – each partner remains an individual?

Our overall concern is that these amendments to the Rules continue the trend towards ever more onerous collection, verification, record keeping and reporting requirements about the personal information of most individuals in Australia, including their financial affairs. These concerns are compounded by the fact that the enhanced CDD requirements are justified by reference to opinions about the adequacy of the Australian regime of the FATF – a largely unaccountable international organisation of uncertain legal status. While the Australian Anti-Money Laundering and Counter-Terrorism Financing (AML/CTF) Act provides the framework for the requirements in the Rules (which are themselves legislative instruments theoretically subject to disallowance), it is most unsatisfactory that detailed requirements for privacy intrusion are being determined effectively by a group of officials from many different countries, without the normal processes associated with legislated obligations. There is in effect a 'democratic deficit' surrounding the entire AML/CTF regime.

There is also a question mark over the validity of the claims by FATF which are used to justify these Rule changes. We note that an Australian Institute of Criminology Report in 2012 found 'the scope of the formal regime in Australia exceeds the others' (in other jurisdictions studied) in some respects[2].

We are aware that the statutory review of the legislation is commencing soon, and that this is probably the best forum in which to raise our more general concerns about the regime. But it also prompts the question; Why do the Rules need to be amended prior to the imminent review? The answer is no doubt the rationale given in the Explanatory Statement; i.e. 'to address deficiencies with the Australian AML/CTF regime which have been identified by the Financial Action Task Force (FATF)'. However, all this does is re-inforce the conclusion that Australia is subservient to the unelected, unaccountable FATF, even to the extent of pre-empting the statutory review.

We are also conscious of the reality that the 'requirements' imposed in relation to AML-CTF are of incidental benefit to other government agencies such as the ATO, and ASIC, which might find it more difficult to obtain authority for such privacy intrusive requirements based solely on domestic considerations. The extent of surveillance of the financial affairs of everyone in Australia that results from the AML/CTF regime, which has always been disingenuously 'sold' as necessary to combat terrorism and serious and organised crime, means that much more information is available to a wide range of government agencies for use in relation to a much wider range of administrative purposes including routine tax and benefit administration as well as minor law enforcement. This effect is achieved not just by the information required to be reported to AUSTRAC – vast though that is. It is also a result of the Know Your customer (KYC) and record keeping requirements of the AML/CTF law which ensure that an even greater vault of personal information not necessarily required for the business purposes of financial institutions is held for lengthy periods and available to a wide range of government agencies using powers under other laws. This issue has taken on a new salience in light of the worldwide debate about the appropriate limits of state surveillance, following the Snowden revelations about access to telephone records by US, and Australian, intelligence agencies.

[2] Australian Institute of Criminology (2012) *Anti-money laundering and counter-terrorism financing across the globe: A comparative study of regulatory action* (RPP 113) by Julie Walters, Carolyn Budd, Russell Smith, Kim-Kwang, Raymond Choo, Rob McCusker & David Rees

The AML/CTF regime has been a classic case study in 'function creep' and 'scope creep', which are pernicious phenomena that in many areas have diminished individual privacy in Australia over the last few decades.

The proposed amendments

Many of the amendments address perceived 'deficiencies' in the Australian regime identified by the FATF. While the International Standards, and the Australian regime, purport to take a 'risk based' approach, there is a built-in contradiction that prevents this approach from limiting the level of privacy intrusion. This is because Reporting Entities (REs) are expected to know a great deal about their customers before they can make an assessment about the level of risk attached to any specific customer. In effect, this reverses the onus of proof – everyone is assumed to be potentially involved in unlawful conduct, necessitating the same level of information collection. There seems to be very limited 'benefit' to individuals subsequently assessed as being 'low risk' – they have already been subject to the same base level of privacy intrusion.

The amendments do nothing to alleviate this unsatisfactory situation, but instead compound it, by expressly requiring more information about 'beneficial ownership' and 'the purpose and intended nature of the business relationship'

Beneficial ownership

Clearly most individual customers in financial transactions are acting on their own behalf.

We are not sure if one aspect of the changes may offer some hope that the regime is not as intrusive as it might appear in relation to beneficial ownership. Rule 4.12. 2(1) states that '**in the case of a customer who is an individual and who the reporting entity has reasonable grounds to believe is not acting on behalf of another person, the reporting entity may assume that there is no other beneficial owner of that customer.** The Explanatory Statement reverses the wording: 'reporting entities may assume that a customer who is an individual and the beneficial owner of that individual are one and the same, unless the reporting entity has reasonable grounds to consider otherwise.'(ES Page 7). It is not clear what 'reasonable grounds' means in this context and what the practical effect will be – can REs assume that most individual customers are not acting on behalf of a beneficial owner or do they need to collect some evidence that this is not the case, such as an assertion by the customer? If the latter, this would be highly objectionable. At the very least, clearer guidance should be given about this requirement.

Purpose and intended nature of the business relationship

One FATF criticism of Australia's regime is that it fails to adequately require REs to 'understand and, as appropriate, obtain information on the purpose and nature of the business relationship' (FATF Recommendation 10(c)). The Explanatory Statement says that this is addressed in the new rules by a requirement in the Rules that 'reporting entities must understand the business or occupation of the customer'

The requirement is implemented in new Rule 8.1.5 which requires all REs to design their standard AML/CTF Programs to enable them to: '**understand the nature of the business or occupation of each customer'** (8.1.5(1) and to identify **'changes arising in the nature of the business, occupation … of any customer** (8.1.15(4)(d).

These obligations apply in respect of *all* individual customers and in effect requires REs to understand much more not just about the financial affairs of their customers but also about the objectives and lifestyles that those affairs support.

This intrusion is compounded for individuals subject to Enhanced Customer Due Diligence (ECDD) as a result of a high ML/TF risk assessment, with additional enquiries about the source of wealth and source of funds of the customer, and enhances monitoring. But at least there have to be grounds for these additional requirements, which is more consistent with the purported risk based approach.

We submit that imposing additional requirements on REs to pry into the lives of all their individual customers, without any evidence of wrongdoing, is simply unacceptable. It is based on an over-zealous interpretation of the risk based approach, both by FATF in its Recommendation 10 (c) and by AUSTRAC and the Australian Government in their response to the recommendation.

We note that the privacy impact assessment (PIA) of the proposed changes conducted in late 2013 (draft report January 2014) includes recommendations that relate to the source of funds:

> 'Firstly, it may be possible to limit the requirement to collect information on source of funds and source of wealth. This could include restricting it to certain types of Reporting Entities or to certain types of transactions.
>
> Secondly, AUSTRAC should consider developing some guidance on how the information is collected. For example, if AUSTRAC is satisfied for information to be categorised in very broad categories (e.g. occupation types, investment types) then this may allay consumer fears.
>
> Thirdly, …' (Recommendation 7 – see also Recommendation 4)

This recommendation is consistent with our concerns, even though it is based on an assessment of compliance with the notification principle in the Privacy Act (APP5) and is more concerned with customer perceptions than with the underlying intrusion[3]. We strongly support this recommendation and in particular urge AUSTRAC to limit the requirement to collect information on sources of funds/wealth.

[3] The draft PIA report is disappointingly silent on the issue of 'proportionality' in relation to compliance with APP3 – which requires that collection of personal information be 'reasonably necessary'

Relationship to Privacy Act

We note the inclusion in the Rules (in various places including at the end of Chapter 4) of the statement: *'Reporting entities should note that in relation to activities they undertake to comply with the AML/CTF Act, they will have obligations under the Privacy Act 1988, including the requirement to comply with the National Privacy Principles, even if they would otherwise be exempt from the Privacy Act. For further information about these obligations, please go to http://www.oaic.gov.au or call 1300 363 992.'*

While we welcome the inclusion of this reminder[4], it is of limited value without further explanation as to the practical effect in relation to CDD requirements. For example, the obligation under APP 3.2 to only collect personal information that is 'reasonably necessary for one or more of the entity's functions or activities' pushes REs in one direction (of minimising collection) while the discretion left to them under the AML/CTF regime pulls them in the other (maximising collection to ensure they satisfy the Rules).

We submit that the balance between these competing obligations is wrong and is being made worse by the proposed Rule changes.

We note that the draft PIA report commissioned by AUSTRAC provides some support for our position, although predictably, given its terms of reference, it fails to address the underlying problems with the AML/CTF legislation. Any privacy intrusion, however objectionable, can be consistent with the Privacy Act if it is 'required or authorised by or under law', as is the case with the AML/CTF regime. The draft PIA regrettably, but understandably, avoids the issue of whether information collection under the AML/CTF regime is 'proportional' to the objectives and public interests involved – that judgment is assumed to have been made by the legislation.

We also submit that the Rules should more clearly remind REs of the specific obligations under APPs 1.3 and 5 to be clear and public about collection use and disclosure practices. APF has repeatedly made submissions to the effect that in our view, Reporting Entities have not been complying fully with their obligations under the existing NPP 1.3 to notify customers about the AML/CTF collection requirements. We have also consistently argued that AUSTRAC has at least a moral obligation to remind REs of these obligations. Under the new APPs, the notification requirements are enhanced, and there will also now arguably be a stronger legal obligation on AUSTRAC under APP 5.1(b) to ensure customers of REs are aware that some of the information collected may be reported – initially to AUSTRAC but in effect to more than 30 other agencies.

[4] For which we claim some credit, having consistently argued for inclusion of such reminders through our long-term membership of the AUSTRAC Privacy Consultative Committee.

Conclusion

We submit that some of the proposed changes to the Rules significantly increase the level of intrusion into the financial privacy of every individual in Australia, without any evidence that such an increase is actually necessary or that it is likely to achieve any significant benefit in terms of the objectives of the AML/CTF regime.

The changes appear to being made simply to satisfy an arbitrary and unsubstantiated assessment by the FATF – an unelected and unaccountable international body, that Australia's AMML/CTF regime is inadequate.

Given that a wider statutory review of the AML/CTF Act has now commenced, we believe it is premature to make these changes. We submit that at least those amendments affecting individual customers about whom there is no prior reason to be assessed as 'high risk' be withdrawn, pending the outcome of the statutory review in 2015.

If the amendments do proceed, we submit that they should be modified to reduce the level of intrusion in respect of 'ordinary' individual customers – and specifically that the requirements for routine collection of information about 'beneficial ownership' and 'purpose and nature of the business relationship' be relaxed, except for individuals about whom there is justified prior suspicion.

For further information please contact:

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