FINANCIAL ADVICE ASSOCIATION AUSTRALIA

Senator Nita Green
Chair
Senate Legal and Constitutional Affairs Committee
PO Box 6100
Parliament House
Canberra ACT 2600

14 October 2024

Dear Senator

Anti-Money Laundering and Counter-Terrorism Financing Amendment Bill 2024

The Financial Advice Association of Australia (FAAA)[1] welcomes the opportunity to provide input into the Senate Legal and Constitutional Affairs Committee inquiry into the Anti-Money Laundering and Counter-Terrorism Financing Amendment Bill 2024 (the Bill). The Bill serves to modernise the Anti-Money Laundering and Counter-Terrorism Financing (AML/CTF) Act and Rules, and to introduce Tranche 2 to extend the regime to certain professional service providers.

The AML/CTF regime provides vital protection for all Australians and businesses from the risks and impacts associated with money-laundering and terrorism financing (ML/TF).

The FAAA's submission primarily considers the ML/TF risks faced by entities that only provide 'item 54 designated services' – ie. Australian Financial Services Licensees (AFSLs) and authorised representatives providing financial advice – and their clients. We support the intent of the proposed changes to simplify the AML/CTF regime to improve its efficiency for the regulated community and its effectiveness in protecting Australians.

At the time of the introduction of the AML/CTF regime, the financial advice market was predominantly made up of large financial institutions holding AFS licences. There has been a noticeable shift with the major banks, Macquarie, Insignia and AMP all exiting or significantly reducing their footprint in the financial advice market over recent years. Small licensees now make up the largest portion of the advisory market. These small businesses do not have the luxury of AML/CTF in-house experts previously relied upon during the

[1] The Financial Advice Association of Australia (FAAA) is the largest association representing the financial advice profession in Australia, with over 10,000 members. It was formed in 2023 following the merger of the two leading financial planning/advice bodies in Australia – the Financial Planning Association (FPA) and the Association of Financial Advisers (AFA). With this merger, a united professional association that advocates for the interests of financial advisers and their clients across the country was created.

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establishment of the regime and will require time as well as adequate guidance and support from the Regulator to ensure a clear understanding of the intent of their obligations under the Bill.

We welcome the continuation of the 'special program' exemptions for reporting entities that provide item 54 designated services only. However, we are concerned that the Bill was tabled in Parliament without the benefit of consultation on exposure draft legislation. This is a substantial piece of legislation that is critical for the protection of Australians. It will also have significant ramifications for entities that provide item 54 designated services if they are unintentionally caught by the new designated services putting their exemptions at risk.

While we appreciate the principles-based nature of the Bill, it is challenging to assess the implications of the changes to the regime in the absence of draft Rules and guidance. The inclusion of Rule-making powers allowing the creation of exemptions from the new definitions and certain provisions in the Bill will help minimise the risk of unnecessary regulatory overreach.

In our submission we have addressed the need for greater clarity around the:

- application of AML/CTF policies within a business group
- intended coverage of the new professional service definitions to avoid regulatory duplication, and
- intended meaning of terminology included in the professional services definitions that is commonly used within the financial advice profession.

We would welcome the opportunity to discuss the matters raised in our submission with the Committee. If you have any questions about our submission, please do not hesitate to contact either myself on 02 9220 4500 or phil.anderson@faaa.au, or George John, Senior Manager, Government Relations & Policy on george.john@faaa.au or 0420 301 501.

Yours sincerely,

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Financial Advice Association of Australia (FAAA)

FINANCIAL ADVICE ASSOCIATION AUSTRALIA

ANTI-MONEY LAUNDERING AND COUNTER-TERRORISM FINANCING AMENDMENT BILL 2024

Effective date: 14/10/2024
Submitted to: Senate Legal and Constitutional Affairs Committee

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Part 1A AML/CTF Program

Exemptions for item 54 designated services

The FAAA welcomes and supports the retention of the existing exemptions for reporting entities that provide item 54 designated services only, as clearly stated in the Explanatory Memorandum to the Bill:

> *Reporting entities that only provide item 54 designated services will retain their exemption from certain AML/CTF program obligations. This exemption is provided in new section 26T of the AML/CTF Act (to be inserted by Item 24 of this Schedule). Any business that provides a designated service in addition to providing an item 54 service must comply with the full range of AML/CTF obligations for those services.*[2]
>
> *New section 26T maintains the existing exemption for holders of an AFSL that only provide designated services covered by item 54 of table 1 in section 6 (for example, financial planners). These reporting entities are only required to undertake an ML/TF risk assessment, and develop and implement AML/CTF policies that deal with how the reporting entity undertakes initial CDD. This maintains the effect of the previous 'Special Anti-Money Laundering and Counter-Terrorism Financing Programs' under section 86 of the AML/CTF Act.*[3]

What is an AML/CTF program?

Section 26B of the Bill defines an AML/CTF program as comprising:

> a) *the reporting entity's ML/TF risk assessment; and*
>
> b) *the reporting entity's AML/CTF policies.*

Based on the item 54 exemptions under s26T, it would appear the following obligations in relation to ML/TF risk assessments would still apply to item 54 reporting entities:

- to undertake an ML/TF risk assessment (s26C)
- review and update ML/TF risk assessment (s26D)
- must have an up-to-date risk assessment before providing a designated service (s26E)
- ML/TF risk assessment and AML/CTF policies, including any updates, to be (1) approved by a senior manager of the reporting entity and (2) notified to the "governing body of the reporting entity" (s26P).

We note that item 8 of the Bill will introduce a new definition of 'governing body' into s5 of the Act. However, s26T exempts reporting entities that provide item 54 designated services only from the governing body

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[2] Explanatory Memorandum, paragraph 40

[3] Explanatory Memorandum, paragraph 136

obligations in s26H. The application of s26P(2) to these reporting entities will likely cause some confusion, therefore increasing the risk of unintentional breach. This is concerning given s26P is a civil penalty provision.

The FAAA recommends that reporting entities that provide item 54 designated services only should be exempt from s26P(2) of the Bill as they are exempt from the obligation to have a governing body.

Item 54 exemptions for reporting entities within a business group

Section 26G of the Bill states:

> 1) *A reporting entity must comply with the AML/CTF policies of the reporting entity.*
>
> 2) *If:*
>
>   a) *a reporting entity is a member of a reporting group; and*
>
>   b) *the reporting entity is not the lead entity of the reporting group;*
>
> *the reporting entity must also comply with the AML/CTF policies of the lead entity of the reporting group that apply to the reporting entity.*
>
> *Note: The lead entity of the reporting group must comply with its own AML/CTF policies under subsection (1).*

The inclusion of the words *".....that apply to the reporting entity*" in s26G(2)(b) imply that the reporting entity need only comply with those AML/CTF policies that they are obliged to meet under the Act, not all the AML/CTF policies of the lead entity of the group. Meaning that if exemptions from Part 1A apply to a reporting entity that is a member of a group (but not the lead entity), those exemptions continue to apply.

Under s26T of the Bill, reporting entities that provide item 54 designated services only are exempt from specific provisions in Part 1A relating to AMLCTF programs. Item 54 reporting entities are holders of an Australian Financial Service Licence (AFSL). AFSL holders may be a subsidiary company of a corporate group. The law should clearly permit the legal entity holder of the AFSL that only provides item 54 designated services, to maintain the Part 1A exemptions, including when the reporting entity is part of a business group. The additional AML/CTF obligations of the broader business group should not be forced upon the subsidiary item 54 reporting entity. This would unfairly impose an additional regulatory burden on one set of AFSL holders based on their business model, creating a competitive disadvantage.

This approach mirrors the application of the current AML/CTF obligations where a business group may provide multiple designated services and a separate legal entity, within the group, holds the AFSL and is registered with AUSTRAC as a 'item 54 only reporting entity'. The current 'special program' exemptions apply to such entities.

The FAAA supports the implied meaning of s26G(2)(b) however this should be made clear in the Explanatory Memorandum to the Bill.

The FAAA recommends paragraphs 107 and 108 of the Explanatory Memorandum specifically state that:

- the exemptions that apply to reporting entities that provide item 54 designated services only continue to apply to such entities that are part of a business group, and

- reporting entities that provide item 54 designated services only and are part of a business group, need only comply with those AML/CTF policies that they are obliged to meet under the Act, not all the AML/CTF policies of the lead entity of the group.

General exemptions

The Bill inserts new general exemption provisions under s26V and provides the power to include in the AML/CTF Rules exemptions to designated services from Part 1A – AML/CTF Programs. FAAA supports this power as it will provide a mechanism to address unintended consequences of the new obligations and emerging issues.

Part 2 – Customer due diligence

Monitoring unusual transactions and behaviours

The Bill introduces modernised ongoing CDD obligations and most notably a requirement to monitor for "*unusual transactions and behaviours*" of a customer, which is defined in s30(5). While s30(10) provides a clear exemption from the provisions of s6 for reporting entities that provide item 54 designated services only, we are concerned about the implications for AFS licensees and financial advisers acting under a third party reliance agreement with a product provider.

In the absence of finalised Rules and guidance it is unclear how the monitoring of "unusual transactions and behaviours" of a customer would apply between two entities – one that is exempt from this obligation - operating under a third party agreement. In practice, this definition will be applied differently by advisers and product providers, purely due to the different nature of the relationship each has with the client – ie. the adviser-client relationship is different to product-customer relationship – and the different designated services each reporting entity provides. As such, we believe it would be inappropriate for product providers to rely on financial advisers to monitor for "unusual transactions and behaviours" of a customer on behalf of a product provider. Each type of reporting entity should be responsible for their own customer monitoring based on the type of customer relationships they hold and the designated services they provide.

While third party reliance provides certain efficiencies for clients, these arrangements can create tension from product providers requesting additional and ongoing CDD of advisers (who are exempt from such obligations) even when there is no change in the client's circumstances and no SMR event.

The FAAA recommends the Bill exclude the monitoring of "unusual transactions and behaviours" of a customer from third party reliance arrangements.

Simplified and enhanced CDD

The FAAA supports the introduction of simplified and enhanced customer due diligence obligations for low and medium/high ML/TF risk customers, respectively. We would welcome guidance from AUSTRAC on the operation of these CDD obligations.

Part 3 - New designated services

Financial advice terminology and duplication of AML/CTF Act coverage

Tranche 2 introduces a range of new designated services into the AML/CTF regime. While the intent is to regulate activities that pose a high ML/TF risk to Australians, the breadth of the new definitions makes it unclear whether some entities and/or services will be unintentionally captured by the new designated services.

This is a critical issue for reporting entities that provide item 54 designated services only as it puts them at risk of losing the exemptions from Part 1A obligations.

Below are examples of activity conducted in the course of providing an item 54 designated service (ie. a reporting entity, in the capacity of a holder of an AFSL, making arrangements for a person to receive a designated service, other than a service covered by that Item) that pose a low ML/TF risk but may unintentionally be captured by a new tranche 2 designated service.

These are examples of services that may, from time to time, be requested by a client in certain circumstances. Such services are typically peripheral to the main service the financial adviser provides, being item 54 designated services, and are not a primary activity. Advisers are often the secondary intermediary, not the primary service provider of these new professional services. However, the terminology used in the Bill is unclear and risks advisers being unintentionally captured, particularly in relation to the meaning of 'assisting' and 'planning' for a client. The premise of providing financial advice is to 'assist' the client and provide the client with a 'plan' to meet their financial objectives and needs. These professional services are highly regulated under the Corporations Act and ASIC and present a low ML/TF risk.

As demonstrated by the examples below, the activity undertaken by financial advisers is already covered by item 54 designated services. We question whether it is the policy intent of the introduction of tranche 2 services to also capture financial advice in the new professional services definitions.

To avoid regulatory uncertainty and unnecessary regulatory burden, we ask for care to be taken to ensure the same activity is not inadvertently captured under more than one professional service.

The FAAA recommends the Bill and Explanatory Memorandum, Rules and AUSTRAC Guidance, make it clear that the provision of financial advice is not intended to be covered by the new professional services definitions, namely items 1, 2, 3, and 6.

Item 1 Professional Services

The Bill introduces item 1 professional service that involves 'assisting a person in the planning or execution of a transaction, or otherwise acting for or on behalf of a person in a transaction to sell, buy or transfer real estate in the course of carrying on a business.

As referenced in the EM, this definition is intended to extend the AML/CTF regime to certain services provided by real estate professionals who conduct the buying and selling of real estate. However, this definition may unintentionally capture financial advisers.

For example, if a client suddenly and unexpectedly needs to enter residential aged care and seeks the assistance of their financial adviser to help them decide whether to sell their home to fund the aged care service. The adviser may have a conversation with their client about selling the property and may assist in arranging for the selling of the property. Often this will happen at a time when the client has reduced capacity to represent themselves and they may not have family to assist them. This activity could include the consideration of and advice on the financial implications of keeping versus selling the property along with social security and CGT implications. These conversations are critical to Australians making financial decisions on whether to sell or keep their home at this emotionally charged later stage in life, when the clients are much less capable. The transaction of the property sale is conducted by the real estate agent, not the adviser, who will otherwise be captured in the tranche 2 reforms.

This is not the 'core business' of the adviser, and arguably they are not carrying on a business related to buying, selling and transferring real estate. The focus of the financial adviser's services is to ensure the client's financial objectives are being addressed, including evolving aged care needs as in this example. However, it is unclear as to the extent to which the actions of a financial adviser maybe classified as "assisting" a client. .

Ensuring their financial advice is in the best interest of the client is a requirement under the Corporations Act. We request that care be taken to ensure the AML/CTF regime change does not restrict the ability of financial advisers' to meet the needs of their clients and the adviser's obligations under the Corporations Act and legislated Financial Adviser Code of Ethics.

In practice, it is unclear as to the difference between a financial adviser "making arrangements for a person to receive another designated service" and "assisting" a client with their advice needs.

The FAAA recommends the Bill and EM clearly differentiate between the act of "making arrangements for a person" and "assisting" a person. Financial advisers should not be caught by this item merely for advising their clients on selling a home as part of planning for their future, including transitioning into an aged care facility.

Item 3 Professional Services

Section 5B defines the new item 3 professional service as:

receiving, holding and controlling (including disbursing) or managing a person's:

- *a) money; or*
- *b) accounts; or*
- *c) securities and securities accounts; or*
- *d) virtual assets; or*
- *e) other property;*

as part of assisting the person in the planning or execution of a transaction, or otherwise acting for or on behalf of a person in a transaction, in the course of carrying on a business (other than in a circumstance covered by subsection (5C))

(5C) For the purposes of item 3 of the table in subsection (5B), the circumstances are as follows:

(a) the money, accounts, securities, securities accounts, virtual assets or other property being held or managed is payment by the person for the provision of goods or services by the business;

(b) both:

(i) the business does not provide any designated services other than the services referred to in item 3 of the table in subsection (5B); and

(ii) the money, accounts, securities, securities accounts, virtual assets or other property being held or managed is for payments reasonably incidental to the provision by the business of a service that is not a designated service;

(c) the money, accounts, securities, securities accounts, virtual assets or other property being held or managed is to be received or payable under an order of a court or tribunal;

(d) the service provided by the business is the receipt or disbursement of a payment mentioned in subsection (5D);

(e) the service is any other designated service;

(f) a circumstance specified in the AML/CTF Rules.

Note: An example of a circumstance to which paragraph (b) applies is fees paid to a barrister for representation in legal proceedings or property management services.

The EM to the Bill states the intent of the new designated service is to ensure the following types of activities are covered by the AML/CTF regime - *where a professional service provider*:

a. *holds sale proceeds or purchase funds for a customer on escrow (which legal practitioners may know as 'transit money')*

b. *money or property is held by a professional service provider prior to being settled as trust property on the creation of an express trust, or*

c. *has authority over a customer's bank account and makes payments from that account on behalf of a customer, for example, to make loan repayments to a financial institution.*

The two determining factors of whether a professional service is covered under the new designated service are:

whether the professional service provider is providing the person with services that are associated with a transaction, whether planning, executing or otherwise acting on behalf of the person, and

whether the professional service provider's interaction with a person's property has an active element (that is, controlling, disbursing or managing).[4]

We note that financial advice as an item 54 designated service is not included in the activity described in the EM as intended to be covered by item 3; and that s5C(e) excludes a service that is *"any other designated service"* from this item 3 professional service definition.

Financial advisers work to understand their clients through extensive fact-finding interviews, in which clients disclose a wide range of personal information including the client's financial position, employment, family ties, health issues, current living arrangements and goals and aspirations for the future, among other things. A financial adviser will then take this personal information and develop financial advice for the client which may recommend an investment strategy, savings plan, insurance arrangements, management of cash-flow, strategies for achieving the client's financial goals, and if appropriate, financial products. The adviser may assist in the implementation of the advice.

However, while it is implied that it is not the intention for item 54 designated services to be captured by the item 3 professional service, the definition in the Bill and the associated paragraphs in the EM lack certainty in this regard. Should such advice services inadvertently be captured, this would duplicate the regulatory coverage of the advice activity and AFSL holders would lose the item 54 exemptions.

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[4] Explanatory Memorandum, paragraph 369

We are particularly concerned that the implementation of advice recommendations – which may involve an element of control but there is no flow of money in or out of a product and therefore present a low ML/TF risk - may unintentionally be caught by this new designated service.

For example, if a client invests funds directly via a wrap account or platform and the financial adviser moves the investment around into different asset allocations within the account to achieve the client's investment goals. The money does not enter or leave the wrap account or platform as a result of the financial adviser's activity. The money going in and out of the wrap account or platform is from the account to the client. Given the adviser is not transacting or disbursing funds, we suggest this activity presents a low ML/TF risk. There are many similar examples where client funds are retained within a structure or financial product and the adviser moves the funds around to maximise the investment, such as superannuation and investment bonds.

In other circumstances, a financial adviser who is working with an elderly client, might be asked to ensure that their bills are paid as and when they arise. This is not a primary service, but one that they are forced to provide as their elderly client starts to lose capacity and may no longer be capable of doing this, or may not have a friend of relative to pay the bills on their behalf.

We suggest that it is not the intent for the new item 3 professional services to capture this financial advice activity and that this should be made clear in the EM, Rules and AUSTRAC Guidance.

It is unclear as to the difference between a financial adviser "making arrangements for a person to receive another designated service" and "assisting" a client with their advice needs.

The FAAA seeks clarification on the ML/TF risk and professional service activity item 3 is intended to cover.

Item 2 and 6 professional services

The Bill proposes to introduce item 6 professional service:

> *assisting a person to plan or execute, or otherwise acting on behalf of a person in, the creation or restructuring of:*
>
> *(a) a body corporate (other than a corporation under the Corporations (Aboriginal and Torres Strait Islander) Act 2006); or*
>
> *(b) a legal arrangement;*
>
> *in the course of carrying on a business*

Fundamental to the provision of financial advice is "assisting a client to plan" for their financial circumstances, goals and future. As part of this activity, financial advisers may advise a client on the benefits and suitability of establishing a Self-Managed Super Fund (SMSF). An SMSF, which is a trust, is usually accompanied by the establishment of a corporate trustee. The role of the adviser would be limited to:

- recommending the client establish a SMSF
- recommending the client establish a corporate trustee for the SMSF
- advice on the investments inside the SMSF
- and then at a later point, when no longer suitable, recommending the client close the SMSF.

The financial adviser would refer the client to an accountant to execute the establishment and closure of the SMSF and corporate trustee. The provision of the financial advice in relation to the SMSF is to 'assist' the client with a 'plan' to achieve their retirement goals.

We are concerned that the provision of a Statement of Advice (SOA), which is an obligation under the Corporations Act and is considered the client's 'financial plan', could result in SMSF financial advice being captured by the definition of item 6. This would be duplicative regulation as the provision of the advice (ie. the "arranging" for the accountant to execute the establishment of the SMSF) is already covered under the item 54 designated service.

SMSFs are also heavily regulated structures under the SIS Act and should not pose a high ML/TF risk.

Similarly, financial advisers may advise a client regarding circumstancing involving the change in membership of a SMSF, which may result in the need to transfer the ownership of a SMSF corporate trustee. Given item 2 professional service is defined as *"assisting a person in the planning or execution of a transaction, or otherwise acting for or on behalf of a person in a transaction, to (c) transfer a body corporate or legal arrangement",* we are concerned that this advice activity may be caught under this new definition. Once again, the adviser would assist in the planning as part of their advice recommendation.

The FAAA recommends the Bill and EM make it clear that the provision of financial advice is not covered by items 2 and 6 professional services.

Rules making powers

Given the significant range of the tranche 2 designated services being introduced, identifying low ML/TF risk activity that may be unintentionally captured by the new definitions should be an ongoing task that should not be restricted to the Bill and the EM.

The coverage of the new tranche 2 designated services creates uncertainty for all professional service providers but has significant implications for item 54 reporting entities as it puts at risk the exemptions from relevant Part 1A obligations.

The FAAA supports the inclusion of rule-making powers in relation to the tranche 2 designated services, such as those in new subsections 6(5C) and 6(5D) of the Bill, that will allow "*additional exemptions to be made in the AML/CTF Rules in exceptional circumstances and where the exemption provided reflects low money laundering and terrorism financing risk"*.

As this is the first opportunity we have had to assess the Bill, and it will provide a mechanism to address unintended consequences of the new tranche 2 designated services and emerging issues with the changes into the future, we suggest the Rules-making powers be more broadly applied.

Industry specific regulatory guidance

Business activity and practices differ across the professional services sector. How the tranche 2 designated services and the AML/CTF obligations apply to each professional service provider will be based on the services provided and the nuances of each profession.

Industry specific regulatory guidance on the following matters is critical to ensure each profession understands how the AML/CTF regime applies to the services they provide.

- the professional services activities the new designated services are intended to capture, and not capture.
- AML/CTF risk assessments (including reviews and updates) and program requirements.
- the application of the third party provisions to the new customer due diligence requirements.

This includes existing reporting entities that provide item 54 designated services - even though they are not new to the regime, these changes will have a significant impact on their business.

Transition arrangements and ongoing stakeholder engagement

We note that transition arrangements vary for different parts of the Bill:

- AUSTRAC powers and changes to some definitions (eg. credit card/issuer; securities; derivatives) commence – 28th day after Royal Assent.
- The changes to AML/CTF program, CDD, record keeping obligations commence 31 March 2026 for tranche 1 reporting entities.
- Entities that provide the 'new designated services' (tranche 2 entities) may enrol as reporting entities on AUSTRAC's Reporting Entity Roll from 31 March 2026 and must be enrolled with AUSTRAC no later than 29 July 2026; and must meet the regulatory obligations for AML Programs, CDD, professional services (T2) and record keeping by 1 July 2026.

It is difficult to state with certainty whether the transition arrangements are adequate given reporting entities will not have the benefit of finalised Rules and guidance critical to understanding the detail on how they should comply with the new obligations.

The FAAA supports the power given to the Minister to make transitional rules concerning any amendments introduced by this Bill. This modification power is limited to 4 years to address any unforeseen issues that may arise after the reforms commence and to accommodate the extensive time needed for industry to effectively implement each measure. The modification power will allow for adjustments based on ongoing

industry consultations, ensuring that the reform measures and the AML/CTF regime overall remains effective and suitable for the regulated population.

It is critical for the continuation of AUSTRAC's stakeholder engagement forums to continue post-commencement of the new provisions, to inform the Regulator and government of the need for adjustments to ensure the effectiveness of the regime.