FINANCIAL ADVICE ASSOCIATION AUSTRALIA

14 February 2025

Mr Brendan Thomas
CEO
AUSTRAC
PO Box K534
Haymarket NSW 1240

Dear Mr Thomas,

Draft Anti-Money Laundering and Counter-Terrorism Financing Rules 2024

The Financial Advice Association of Australia (FAAA)[1] welcomes the opportunity to provide feedback on the draft Anti-Money Laundering and Counter-Terrorism Financing Rules 2024 (the draft Rules).

The Anti-Money Laundering and Counter-Terrorism Financing (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) and is strongly supported by the FAAA.

Our members are predominantly providers of item 54 designated services, however in our submission we have suggested changes to improve the regime for all reporting entities. An item 54 designated service involves 'arranging' for another designated service and does not directly provide a 'transaction'.

This definition, and the associated ML/TF risks, are reflected in the continuation of exemptions in the Amended Act for reporting entities that only provide item 54 designated services, which are welcome. In our submission we have highlighted areas of concern and where there is a need for greater clarity to ensure the draft Rules and AUSTRAC guidance achieve the legislative intent of the regime, while ensuring these exemptions can be applied in practice.

With the expansion of the regime to tranche 2 reporting entities, which we support, we believe it is important to ensure a practical approach is taken in the Rules and guidance to avoid unnecessary regulatory overload where there is no material or additional ML/TF risk minimisation benefits for Australians. Regard must also be given to the legal responsibilities under relevant laws governing the provision of services to consumers,

[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.

the ML/TF risk of the service to be provided, and the expanded breadth of AUSTRAC's regulated community. There will be, in many cases, multiple reporting entities involved in the delivery of services to consumers, creating regulatory duplication at each point in the supply chain.

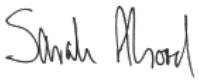
We support the intent of the proposed changes to simplify the AML/CTF Rules to improve its efficiency for the regulated community and its effectiveness in protecting Australians.

In our submission we have addressed a need for greater clarity regarding:

- the intended meaning of terminology included in the tranche 2 designated services definitions that is commonly used within the financial advice profession and by consumers
- the lead entity of a reporting group, and
- the operation of third party reliance.

We would welcome the opportunity to discuss the matters raised in our submission with AUSTRAC. If you have any questions about our submission, please do not hesitate to contact either myself on 02 9220 4500 or sarah.abood@faaa.au, or FAAA General Manager Policy, Advocacy & Standards, Phil Anderson at phil.anderson@faaa.au.

Yours sincerely,



Sarah Abood
Chief Executive Officer
Financial Advice Association Australia (FAAA)

FINANCIAL ADVICE ASSOCIATION AUSTRALIA

Draft AML/CTF Rules 2024

Date of submission: 14/02/2025
Submitted to: AUSTRAC

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Introduction

Both the regulation and provision of financial advice have significantly evolved since the AML/CTF regime was introduced nearly two decades ago. The Corporations Act changes during this time include (for example):

- Banning of conflicted remuneration
- Introduction of a best interest duty
- Professional standards and minimum education obligations - entry requirements including a minimum degree or equivalent qualification, Professional Year, a national exam, and ongoing CPD.
- Introduction of a legislated Code of Ethics
- Enshrinement of the titles “financial planner” and “financial adviser”, legally restricting their use to those who meet the professional and education standards
- Legislated reference checking protocol, including fit and proper person obligations
- Enhanced ASIC powers and the introduction of the Financial Adviser Register
- The establishment of a financial adviser disciplinary body
- Additional requirements for financial advisers who provide tax (financial) advice services.

The financial advice market has also changed. At the time of the introduction of the AML/CTF regime, financial advice firms were predominantly made up of large financial institutions holding AFS licences. There has been a noticeable shift with the major banks, 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 – as at 31 January 2025, there were 1,890 licensees with active financial advisers, and 51% of advisers work in licensees with less than 50 advisers *(Data from the ASIC Financial Adviser Register)*. In terms of advice businesses (P/L structures), the data is even more stark, with 92% of advisers working in businesses with 10 or fewer advisers *(Data from Investment Trends)*. These small businesses generally do not have AML/CTF in-house experts, who were previously relied upon by large businesses during the establishment of the regime. Financial advisers will require time and adequate guidance and support from the Regulator to ensure a clear understanding of their obligations under the AML/CTF reforms.

KEY ISSUES

Designated services definitions and terminology

The new professional services definitions in s6 of the Amended Act include the words ‘assist’, ‘plan’ and ‘execute’. Item 54 reporting entities ‘arrange’, implying that this is different to assisting, planning or executing. This is causing significant uncertainty and concern that the provision of financial advice could be captured by both the item 54 designated service and an additional tranche 2 designated service definition, putting at risk the item 54 exemptions.

We believe it is not the policy intent of the introduction of tranche 2 services to also capture financial advice in the new professional services definitions. However, under the Corporations Act, and in practice in the advice profession, this terminology is heavily used and implies certain activity. For example:

- The titles “financial planner” and “financial adviser” are used interchangeably within the profession. These titles are both enshrined in s923C of the Corporations Act, legally restricting their use to those who meet the professional and education standards. The 'product' provided to clients by financial advisers/planners is in fact the financial plan, rather than a financial product. Pursuant to implementing a financial plan, the financial adviser/planner may ***'arrange'*** for the client to acquire a financial product from a product provider, or seek the services of another professional (such as a legal practitioner to put in place an Enduring Power of Attorney (EPOA)). The word ‘plan’ is inherently in the title and services of the financial advice professional.

- ASIC Regulatory Guide *RG175 - AFS licensing: Financial product advisers—Conduct and disclosure* states the features of good quality advice should include “***assistance*** given by the advice provider to the client, if required, to set prioritised, specific and measurable goals and objectives”.[2]

- The detailed conduct obligations set out in the Explanatory Statement for the legislated Financial Adviser Code of Ethics requires an adviser to provide “detailed engagement with and ***assistance*** to the client”.[3]

- ASIC promotes advice services to consumers through the use of statements including:

    - Financial advisers are professionals who can help you ***plan*** and manage bigger financial decisions.

    - Or ***assist*** you to set more realistic goals.[4]

- When a financial planner/adviser implements a financial plan, they do so by executing the recommendations agreed to by the client.

Importantly, a financial adviser uses these words when describing to a client the services they provide and what financial advice is. Financial advice is commonly described as a professional service that ‘assists’ a client to ‘plan’ for their future.

The terminology used in the Amended Act is unclear and risks advisers being unintentionally captured, particularly in relation to the meaning of ‘assisting’, ‘planning’ and ‘executing’ 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 services are highly regulated under the Corporations Act with oversight by ASIC and present a low ML/TF risk.

The use of these words and phrases in the context of the new professional services are causing significant confusion because they are an inherent part of the financial advice profession. It is unclear where the boundaries of these services fall, and the ML/TF risk they are trying to capture.

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[2] RG175.158

[3] Standard 5, paragraph 44

[4] moneysmart.gov.au

As discussed with AUSTRAC, the FAAA and SMSF Association will provide AUSTRAC with specific examples of tasks that may, from time to time, be conducted in the course of providing an item 54 designated service that pose a low ML/TF risk but may unintentionally be captured by a new tranche 2 designated service because of the use of this terminology. These examples will be provided in the coming weeks.

The Rules, backed up by AUSTRAC guidance, must be clear to enable businesses to make an informed decision about the services they provide to clients, and to feel confident that the assistance they provide clients as part of their financial advice service is just that – financial advice / item 54 designated services. We believe the intent of the regime is not to duplicate regulatory capture of a designated service or business activity.

The FAAA will help our members understand the boundaries of the different professional designated services to ensure they can assess the services they provide clients in the context of the regulatory obligations and make appropriate informed decisions for their business and clients. We would welcome the opportunity to work with AUSTRAC on industry-specific guidance to assist our members.

Recommendations

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

1. The FAAA recommends the Rules and AUSTRAC guidance make it clear that the provision of financial advice is not intended to be covered by the new tranche 2 designated services definitions, particularly items 1, 2, 3, and 6.

Section 8 Lead entity of a reporting group

Under the Corporations Act, financial advice is legally provided by the AFSL holder (often referred to as the licensee). Equally, it is the AFSL holder that is the reporting entity and is legally responsible for the provision of item 54 designation services under the AML/CTF regime. The individual practitioner is not the reporting entity.

The FAAA appreciates and supports the flexibility in s8 for determining the lead entity of a reporting group. Given the diversity of business models in the financial advice profession, determining the lead entity may vary on a case-by-case basis.

It is difficult to provide complete feedback on this section of the Rules in the absence of wording of s8(4) and s8(5). However, we do have the following concerns about the wording in s8(3) of the draft Rules, which states:

> (3) *If more than one person in the group satisfies the criteria in subsection (2), the lead entity is the person that has **the most direct control** of all other members of the group that provide a designated service.*

This provision will likely create significant confusion and uncertainty for financial advisers operating in a multi-disciplinary practice, such as one that provides financial advice, mortgage broking and accounting services. The provision of item 54 designated services – i.e. financial advice provided by an ASIC registered

financial adviser under an AFS licence – is significantly different to the new designated services provided under tranche 2 of the AML/CTF regime, due to the AFS licensing regime in the Corporations Act. While the 'professional' is the registered financial adviser, the legal entity providing the advice is the AFS licence holder, known as the licensee.

A multi-disciplinary small business practice may, for example, include an accountant, mortgage broker and financial adviser, under a variety of different business models. In each business model, the AFS licensee would need to determine not just potential efficiency gains and improvements in client experience, but importantly the privacy, cyber security and business risks associated with the sharing of client data permitted under the AML/CTF reporting group reforms, and any impact these would have on critical business insurances. Consideration would also need to be given as to whether the sharing of client CDD information would be permitted under the financial advice licensing obligations.

Given the complexity of the licensing regime and the different business models used, identifying the members and lead entity of the business and reporting group is complicated.

Legal responsibilities and demarcation

The obligations under the Corporations Act make it clear as to the legal boundaries and responsibilities for the services that are provided. Legally, financial advice is provided through the AFSL holder.

While the AFSL is legally responsible for the financial advice, as the following sample of multi-disciplinary business models demonstrate, depending on the ownership structure of the legal entities involved, the AFSL holder may not be responsible for or have any control over the accounting or other designated services that a multi-disciplinary firm may provide.

Similarly, under the Tax Agent Services Act, the registered tax agent is responsible for the accounting services provided under their Tax Practitioners Board (TPB) registration.

Business model examples

The following examples of multi-disciplinary business models that provide financial advice, supplements the business model examples previously provided in FAAA's response to AUSTRAC's *Out of Session questions on business models*, dated 11 December 2024.

These business model examples serve to demonstrate the complexity of identifying the lead entity of a reporting group.

1. External AFS licensee

The AFS licensee may authorise both corporate authorised representatives (CARs – that is, corporate businesses) and individual financial advisers to provide financial advice under their licence. The CAR may employ financial advisers (authorised representatives) to provide advice under their 'corporate authorised representative' authorisation, and commonly operates as a small financial advice practice/firm. A CAR may be authorised by and thus be a member of a larger corporate group, however as a completely separate and unrelated entity. This is merely an authorisation under the AFS license.

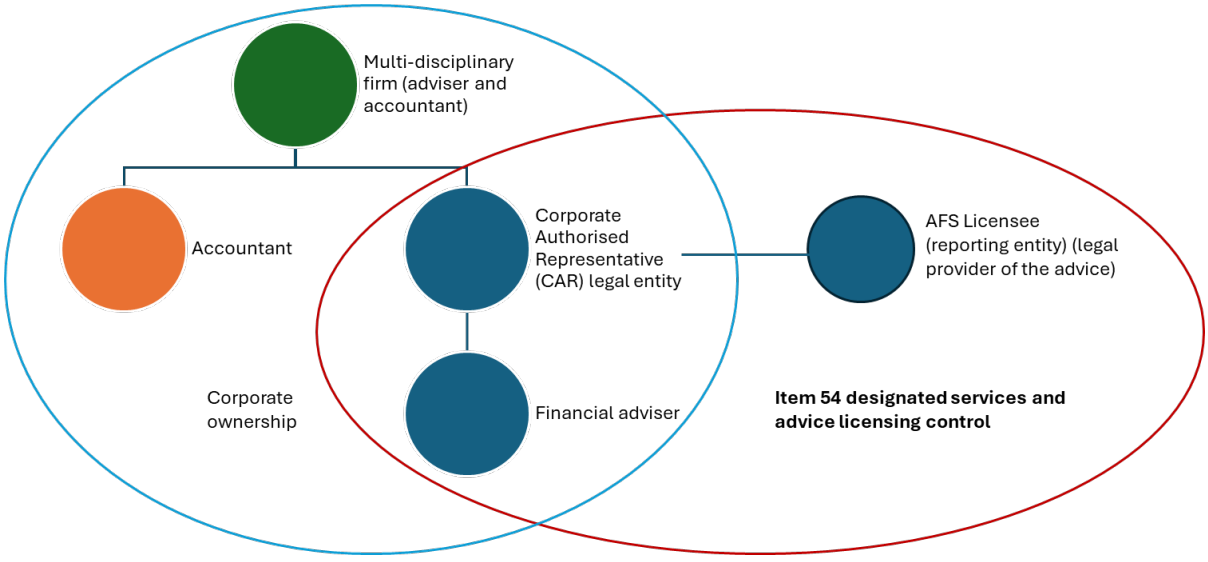
In a CAR context, the AFS licensee may be an external company related only through the financial advice licensing regime, not through ownership, to the legal entity providing the multi-disciplinary services. This AFSL holder may authorise many CARs and advisers under their licence, who operate similar small multi-disciplinary service businesses.

Under this type of business model, some larger external AFSL holders currently strictly 'ring-fence' all client information and data collected under their licence and prohibit the adviser from sharing client identification documentation with other parties within the adviser's multi-disciplinary firm, including for AML/CTF purposes.

This business model demonstrates that the financial adviser and CAR could, as the Rules and Amended Act are drafted, be a member of two reporting groups – that of the multi-disciplinary firm (assuming it is captured by the tranche 2 designated services), and that of the AFS licensee.

However, for this business model, it is legally necessary that all the financial advice related activity of the CAR and financial adviser must sit under the licensee as the AFSL holder and the reporting entity for AML/CTF purposes. The AFSL holder is the AUSTRAC reporting entity and typically only provides item 54 designated services. In this business model, we suggest the CAR (legal entity) would be a member of the AFSL holder's reporting group with the licensee the lead entity.

It is our understanding that a CAR, whilst not being a reporting entity, would be a member of the AFSL holder's reporting group.



2. External AFSL and accountant/adviser practitioner

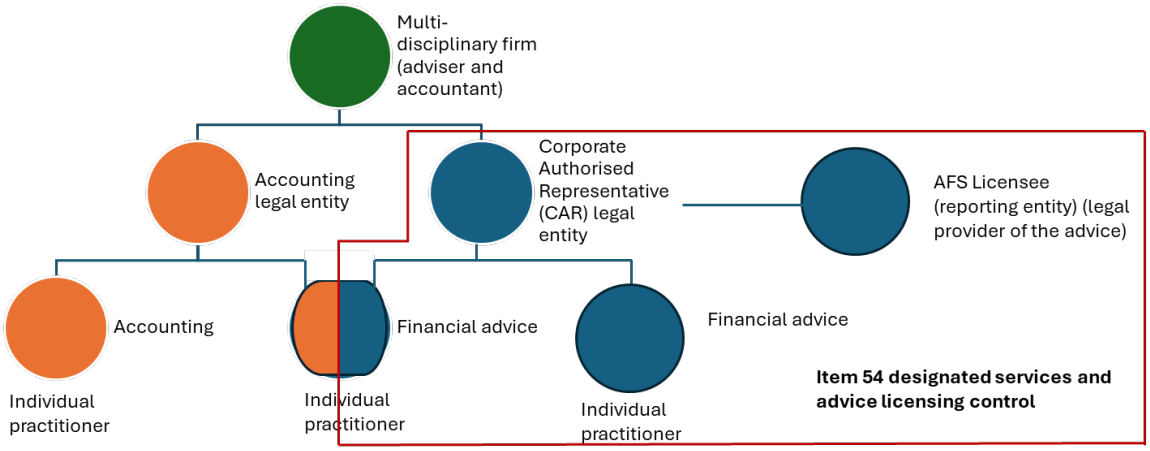
There may be business models where the financial adviser is also an accountant.

This may occur where the individual is operating within a small multi-disciplinary firm, for example. Although provided by a single individual, the financial advice and accounting services are provided through separate legal entities and may rely on separate business systems:

- Based on the item 54 designated service definition in the Amended Act, the financial advice business must operate under an AFS licensee for AML/CTF purposes. The AFS licensee will

authorise a legal entity as the CAR and put in place strict boundaries around the provision of the advice. This may include requiring the financial adviser to use the AFSL's systems and processes, including for AML/CTF purposes related to the provision of the item 54 designated service.

- The accounting services are legally provided by a separate legal entity of the practice. The accountant uses the practice's own systems, including for client ID purposes when providing accounting services.



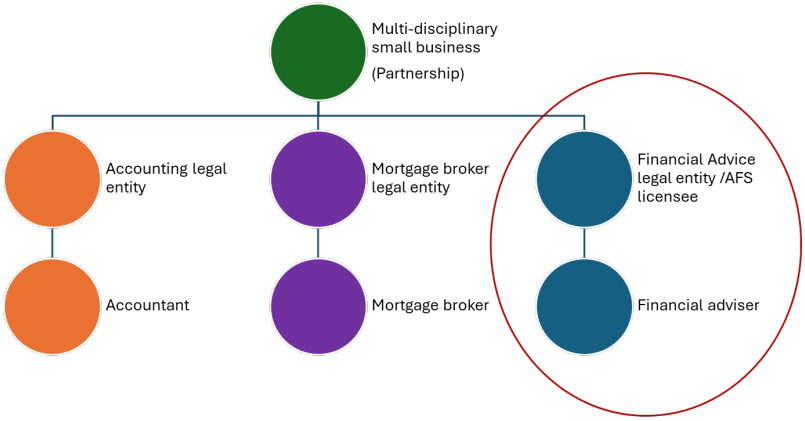
The AFSL holder provides item 54 designated services only. The application of the AML/CTF obligations must reflect these legal requirements and demarcations under the laws relevant to these highly regulated services.

Given the designated service is regulated under the AFSL holder, we suggest the CAR would be a member of the AFS licensee's reporting group, with the AFS licensee the lead entity.

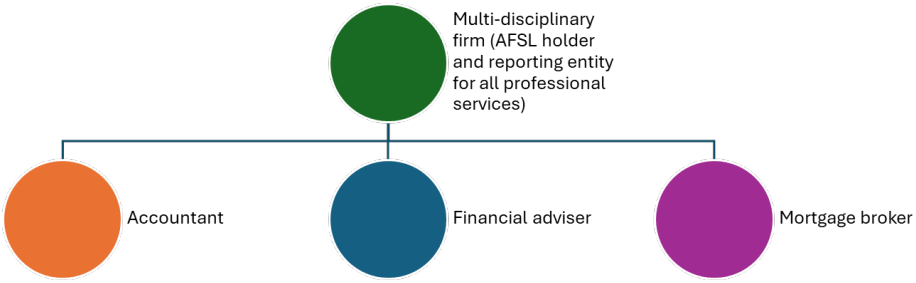
There may be some AFS licensees who authorise financial advisers operating within a multi-disciplinary firm, where the AFSL holder themselves may be a member of a larger reporting group, including where members of the larger reporting group provide different designated services. As shown in example 4 below, the AFSL holder, and CARs operating under their licence, would be a member of the larger reporting group structure. The lead entity in this scenario would likely be the parent company.

3. Boutique / small licensee

Another business structure for multi-disciplinary businesses is for each designated service to be provided by separate legal entities under a partnership arrangement. Under this structure the adviser may be the provider of the item 54 designated service and hold the AFS licence and act as the Responsible Manager and Compliance Officer for advice purposes. The legal entity licenced to provide financial advice would provide item 54 designated services only.



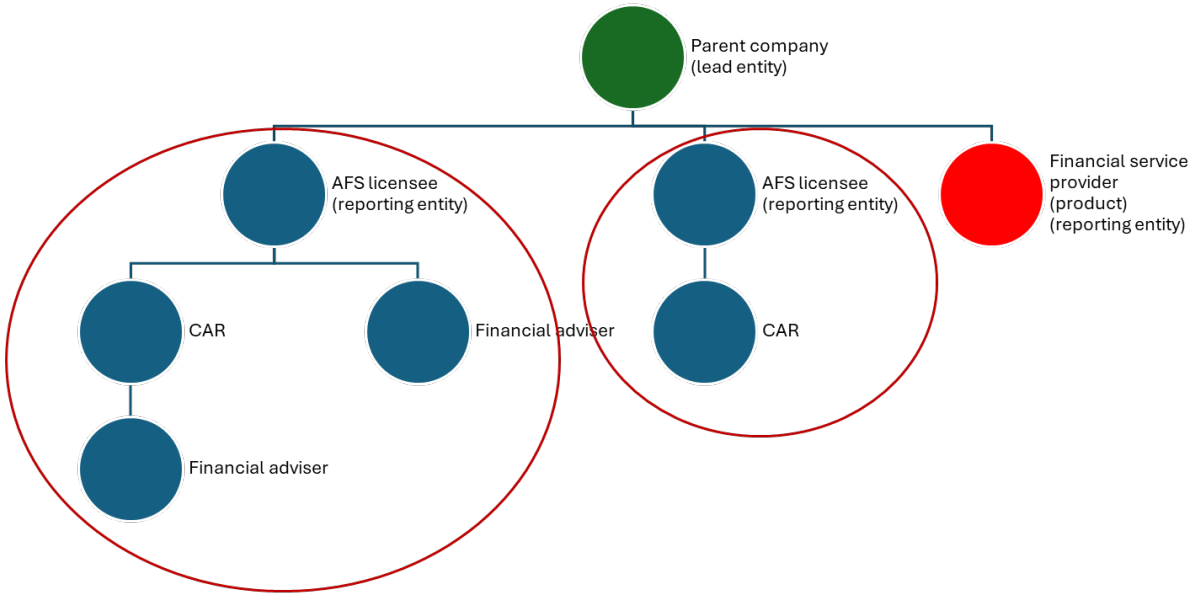
Or a business may have one legal entity that holds the AFSL and legally provides additional services as just one reporting entity for all designated services. It is clear under this type of business model that additional designated services are being provided and the item 54 exemptions would not apply.



The operation of the item 54 exemptions in the AML/CTF regime applying to an AFS licensee that operates within a broader business model that provides additional designated services, is not new. As demonstrated by the example below, a business model that provides multiple services to consumers, including item 54 designated services, is similar in operation to the concept of tranche 1 designated business groups.

4. Dealer groups (Advice AFSLs)

One or more corporate entities in the dealer group will hold an AFS licensee. The licensee(s) may be a separate legal corporate entity within the larger business group. The AFSL holders within the group authorise both corporate authorised representatives (CARs) and individual financial advisers to provide financial advice. There may be more than one AFS licensee within a dealer group. There may also be separate legal entities within the group that provide other financial services/designated services (such as financial products). Generally, we would expect the parent company of the dealer group to be the lead entity for AML/CTF.



Application of item 54 exemptions within a reporting group

These are just five examples of the diverse business models of the advice profession. These demonstrate the need to ensure there is flexibility in the AML/CTF regime to allow for the legal parameters set in the relevant laws that regulate the different professional services, and for businesses to be able to identify the appropriate lead entity.

The AFS licensee is legally responsible for financial advice and is the AUSTRAC reporting entity for item 54 designated services. Critically, as these business models demonstrate, in most businesses the AFS licensee controls the provision of item 54 designated services only. The Rules and AUSTRAC's approach to enforcement must acknowledge this and ensure the item 54 exemptions in the AML/CTF regime continue to apply to all AFS licensees that provide item 54 services only, regardless of which company in a reporting group is the lead entity.

Some AFS licensees may choose to provide more than item 54 designated services under the same legal entity. Guidance on the item 54 exemptions and how they apply, would assist licensees (particularly small businesses) in making this critical business decision.

We understand one objective of the new reporting entity / lead entity / business group provisions is to permit the sharing of client identification data across the business or reporting group. This is a welcome improvement and has the potential to provide significant efficiencies throughout the financial services industry and for clients.

As mentioned above, it is currently common practice for different legal entities within a business group, including AFS licensees, to ring-fence client information to protect data from privacy and cyber security risks, and ensure confidentiality obligations are met. Before permitting information sharing, AFS licensees would need to consider potential impacts on professional indemnity, cyber security and other insurances, as well as their ability to monitor other providers to ensure AML/CTF obligations are met. The sharing of identification information may be problematic with different systems used by different entities, particularly in business

models where the AFS licensee is external to the multi-disciplinary firm. The AFS licensee would also need to consider this alongside their obligations in the Corporations Act.

Definition of control

We note that the reforms include a definition of control, which is central to determining the lead entity under s8(3) of the Rules. However, control is also defined in other laws relevant to AUSTRAC's regulated population. For example:

- s 50AA of the Corporations Act defines the meaning of control, which includes where the first entity controls a second entity if the first entity has the capacity to determine the outcome of decisions about the second entity's financial and operating policies.

- ATO Automatic exchange of information guidance – CRS and FATCA defines 'Controlling person' for an individual, company, trust and partnership.

It would be helpful if there was greater certainty of the alignment of these definitions.

Recommendations

The FAAA recommends that:

2. The Rules and AUSTRAC guidance make it clear that there is flexibility to choose the appropriate lead entity of a reporting group.

3. The wording in s8(3) of the draft Rules - that the lead entity is the entity that has "the most direct control of all members of the group" – be considered and clarified in line with the legal obligations and licensing regime in the Corporations Act for financial advice; as well as other legal definitions of 'control'.

4. The Rules regarding reporting entities should make it clear that the item 54 exemptions continue to apply to the legal entity within the group that holds the AFSL and licenses the advisers operating under its licence, where the AFS licensee (as the reporting entity) provides item 54 designated services only.

We suggest guidance on reporting groups and determining the lead entity in multi-disciplinary firms would be helpful for small businesses. This should include considerations for the sharing of client identification documentation information.

Section 9 - Review of ML/TF risk assessment

We note that s9(1) relates to adverse findings in an independent evaluation report of a reporting entity's ML/TF risk assessment. It is our interpretation of the Act that an independent evaluation report is required under s26F(4) of the Amended Act.

Section 9(2) of the draft Rules requires that "*the review [of the reporting entity's ML/TF risk assessment] must be undertaken as soon as practicable after the governing body of the reporting entity receives the independent evaluation report*".

However, s26T exempts reporting entities that provide item 54 designated services only from s26F(4) of the Amended Act and the obligation to have a governing body in s26H.

The Senate Economics Committee inquiry into the AML/CTF Amendment Bill recommended:

> *…that the bill be amended to ensure uniform exemptions for item 54 entities from governing body requirements* (Recommendation 4).

This recommendation was supported by the government as per its response to the SEC report released in January 2025.

Recommendations

5. The FAAA recommends that reporting entities that only provide item 54 designated services be exempt from s9 of the draft Rules as they are exempt from the obligations for independent evaluation reporting and from having a governing body. As currently drafted, this may cause some confusion, therefore increasing the risk of unintentional breaches.

Section 44 - Third Party Reliance

The third party reliance provisions in the draft Rules must be considered in the context of current practices used under such agreements between product providers and AFS licensees.

While these arrangements may work in relation to initial CDD, the implementation of ongoing CDD obligations and customer risk assessments imposed by product providers on item 54 reporting entities, are extremely problematic, with little regard to the ML/TF risk of the adviser or advice service, the size of the advice business (the large majority of which are small businesses), or the ML/TF risk of the client. This will likely increase under these reforms.

This practice by product providers ignores the fact that financial advice licensees are AUSTRAC reporting entities in their own right. AFS licensees must have, and do have, policies and procedures in place that enable them, and the advisers operating under their licence, to meet their AML/CTF obligations. This includes complying with the obligations to ensure the currency of client identification documentation when a designated service (or additional services) is to be provided. For example, when providing a service such as commencing a managed account, when a client is withdrawing funds from super, and, if necessary, re-verifying ID at an ‘annual financial advice client review’ for clients with an ongoing advice agreement.

It also ignores the know your client (KYC) obligations under the financial advice best interest duty in the Corporations Act and the Code of Ethics, which require advisers to "know" and "understand" the client and their broader interests before they can even provide the advice service. This is an obligation which requires detailed investigation and assists financial advisers to be truly satisfied that the client is who they claim to be, and to assess the ML/TF risk of the client.

Over time, product providers have reportedly over-reached in the ongoing CDD demands they place on advice practices under the auspices of their own AML/CTF obligations, with little regard to the impact of this practice or costs incurred on both the advice practice or the client. While an Item 54 reporting entity is not obliged to conduct ongoing CDD, product providers frequently include these obligations in commercial

agreements or operating procedures obliging the AFS licensee and adviser to carry them out. This creates a significant power imbalance.

The most significant issues with the operation of third-party reliance is that the entity conducting the CDD (the 'other person') is not being relied upon by the other reporting entity (the 'first entity') – product providers do not rely on an adviser's attestation regarding their client's identity - they outsource, rather than rely. Instead, commercial arrangements require that copies of all documentation be collected and held for production on request. This results in the item 54 reporting entity having to collect and store copies of documentation that they would otherwise be able to destroy once verification has been completed, significantly increasing cybersecurity risks for their practice.

Financial advisers are also being used as a mechanism to conduct additional CDD, including when no new designated service is being provided by either party, with the adviser and client bearing the cost of this process.

The changes to the regime do not improve the operation of third party reliance. For example, s44(1)(b) requires the reliance agreement to be primarily focussed on the ML/TF risks of the 'first entity', with consideration to the ML/TF risks of the 'other person' (s44(2)).

> *(b) the agreement or arrangement must be appropriate to the risks of money laundering, financing of terrorism and proliferation financing that the first entity may reasonably face in providing its designated services, taking into account the matters mentioned in subsection (2) of this section;*
>
> *(2) For the purposes of paragraph (1)(b), the matters are as follows:*
>
> *(a) the nature, size and complexity of the other person's business, including:*
>
> *(i) the products and services offered by the other person, and the delivery channels by which it provides services; and*
>
> *(ii) the kinds of customers that the other person has;*
>
> *(b) the country or countries in which the other person operates or of which the other person is a resident.*

Current practice indicates that little consideration is given by product providers to the characteristics of the AFS licensee outlined in s44(2).

Section 44(1)(d) of the draft Rules states that:

> *the agreement or arrangement must enable the first entity to obtain copies of the data used by the other person to verify KYC information in accordance with paragraph 28(3)(d) of the Act immediately or as soon as practicable following a request from the first entity;*

We request clarity on the following practical matters in relation to this provision:

- *'obtain copies of the data'* – many product providers currently insist on certified copies of identification. This is costly and ignores technological developments that facilitate verification of

identification documentation. We recommend that AUSTRAC make it clear that certification of identification documents is not required.

- *'copies of the data used to verify'* – we believe this wording is open to interpretation and could unintentionally limit the use of digital technology solutions for CDD. Digital technology offers solutions to the significant cyber security and privacy risk created by the current third party reliance practices of product providers requiring the adviser to provide a certified copy of the client's identification via email or post. The Rules must be technology neutral and provide definitive permission that allows the 'first entity' to rely upon a report generated by a digital identification verification solution used by the adviser. Such technology generated 'client ID&V' reports generally include the client's details (name, address, date of birth, for example), as well as the type of ID document that was sighted by the adviser and the source relied upon for ID verification (such as drivers licence verified through government licensing authority). This allows the first entity to see what data was used by the adviser while improving security for the client and businesses.

There is currently little consistency in what product providers request of advisers and many requests seemingly go beyond what is required in the law. Product providers expect advisers to undertake all CDD requests made by them. This has become a common contractual inclusion in AFSL/product provider distribution agreements which may include unreasonable expectations and demands placed on the adviser/AFSL, with no compensation for costs incurred by the advisers for doing this work.

It is disappointing that the Rules, as drafted, do not serve to address these issues by giving product providers regulatory certainty and clarity that they are permitted to 'rely on' the attestation of financial advisers for ongoing CDD purposes, that the client continues to be who they say they are in circumstances where the client ID remains current.

This issue will likely be exacerbated by the reforms.

For example, it is unclear how third party reliance is intended to operate in relation to the new customer risk assessment obligations. This is an important clarification given these assessments determine whether simplified or enhanced CDD should be applied for both initial and ongoing CDD.

We understand that with the expansion of the regime to tranche 2 reporting entities, the reliance model may apply to other business relationships. The financial adviser experience offers significant insights and lessons to ensure third party reliance obligations work to achieve the intent of the AML/CTF Act and operate in an efficient and effective manner.

Recommendations - Third party reliance regulatory solutions

6. The FAAA recommends the Rules and AUSTRAC guidance outline how a standard reliance agreement should work in practice to improve consistency and cybersecurity, and minimise unnecessary and extraneous costly requests. This should include limits and standards upon what the 'first entity' can reasonably request of the 'other person'. The 'first entity' should be prohibited from placing extra requirements in other commercial contractual arrangements with the 'other person'.

7. The FAAA recommends the Rules clearly permit the 'first entity' (such as financial product providers) to accept and rely upon the attestation of the 'other person' (such as a financial adviser/AFS licensee) for ongoing CDD purposes. This should include permission to rely on:

    a. 'Other person' (Adviser/AFSL) attestation that the client's identification documentation remains current, and the 'first entity' does not need a physical copy of a client's ID if there has been no change in the client's ID documentation, it is still current, and the ML/TF risk of the customer is low.

    b. confirmation that the 'other person' has undertaken a risk assessment of the client and whether the client's ML/TF risk has changed, with clear standardised criteria for what such an assessment entails.

This would significantly reduce cyber security and privacy issues for all parties while achieving the intent of the AML/CTF regime.

An alternative approach would be for the Rules to mandate that the 'first entity' cannot pass-on their ongoing CDD obligations to the 'other person' under a reliance arrangement or agreement if the 'other person' is legally exempt from those obligations, unless the 'other person' agrees.

8. In addition, the FAAA recommends that AUSTRAC clearly state that a 'copy of the data used to verify' could include a report from a digital 'client ID&V' solution rather than requiring a certified copy of the documents themselves.

9. The Rules should permit the 'other person' to recover costs from the 'first entity' for undertaking the CDD, particularly if the 'other person' is legally exempt from the obligations the 'first entity' is requesting. This will go a long way towards addressing the power imbalance between the 'first entity' and the 'other person'. Including cost-recovery permission in the AML/CTF Rules would offer legal provisions to satisfy financial advice conflicted remuneration obligations in the Corporations Act.

These solutions will assist all future reporting entities that will likely operate under a third party reliance agreement.

Section 25 and place of birth

Section 25 of the draft Rules requires a reporting entity to collect a customer's place of birth.

We note s25 only applies to designated services covered by items 1, 3, 5, 29 and 30 of table 1 in section 6 of the Act. Item 54 reporting entities do not provide these designated services, however we are concerned about this information being requested under third party reliance arrangements.

While we appreciate this information is for data analytics purposes to enhance AUSTRAC's ability to detect ML/TF risk, we are concerned about potential customer privacy and discrimination risks stemming from an obligation to collect a customer's place of birth. Place of birth would limit identification documents to passports and birth certificates, which will significantly restrict CDD collection and verification. It may also restrict the financial inclusion of individuals who may not have such documentation.

This is of particular concern given some product providers request certified copies of client identification documentation to be emailed to them.

We appreciate AUSTRAC's acknowledgement that not all consumers will have such records, and that the recently updated guidance on *Assisting customers who don't have standard forms of identification* serves to address such circumstances.

Recommendation

10. The FAAA recommends the removal of the obligation to collect a customer's place of birth.

Monitoring of transactions and behaviours

Section 39 of the draft Rules includes a list of certain kinds of offences against Commonwealth or State and Territory laws. We understand the intent of the inclusion of this list was to narrow the focus of similar provisions in the current requirements, however there is concern around how this requirement will be met in practice given this is a civil penalty provision. Monitoring for such behaviours is a specialty area and resource intensive. This will be a regulatory impost on small businesses, in particular.

While item 54 reporting entities are exempt from this obligation, it is unclear how this may operate under third party reliance agreements.

Recommendations

11. The FAAA recommends AUSTRAC provides specific guidance on expectations for monitoring client behaviours for small businesses.