16 June 2023

Mr Andrew Warnes
First Assistant Secretary
Criminal Justice Division
Attorney-General's Department

Via online portal: consultations.ag.gov.au.

Dear Mr Warnes

COBA response to consultation on modernising Australia's anti-money laundering and counter-terrorism financing regime

The Customer Owned Banking Association (COBA) appreciates the opportunity to contribute to the Attorney-General's Department's (AGD) consultation on simplifying and modernising the Anti-Money Laundering and Counter-Terrorism regime (AML/CTF regime) as well as addressing risks in certain professions.

COBA is the industry association for Australia's customer owned banks (mutual banks, credit unions and building societies). Collectively, our sector has over $160 billion in assets and is the fifth largest holder of household deposits. Customer owned banks account for around two thirds of the total number of domestic Authorised Deposit-taking Institutions (ADIs) and delivers competition and market leading levels of customer satisfaction in the retail banking market.

Key points

COBA does not support **streamlining Part A and Part B into a single program** as currently proposed due to the resulting governance and oversight complexities and inefficiencies. This will be a significant change for COBA's members as Boards and senior management will need to understand Part B requirements, which they have not been required to comply with previously, and it will require the Boards of our members to exercise more oversight of this Program.

COBA is concerned that the removal of **safe harbour** provisions does not account for the difference of risk profiles, organisation size, product, and customer segments across Reporting Entities (REs). Alongside consideration of international examples, like the United Kingdom, COBA strongly recommends that exemption provisions be considered for smaller REs as the safe harbour/simplified customer due diligence provisions are widely used across the customer owned banking sector due to its lower risk profile.

The changes to the **travel rule** must be reconsidered in respect to the acquisition and exchange of payee information as the proposed model is unlikely to be possible in the current landscape.

The wide-ranging impacts of the changes to the AML/CTF regime will require significant implementation and consultation periods on the draft laws and draft guidance from AUSTRAC.

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Clarity will need to be provided on how existing REs will be transitioned to the new regime and whether provisions will apply retrospectively.

Simplifying and modernising the AML/CTF regime

To uphold national security and protect Australia's financial system, COBA agrees that the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) (AML/CTF Act) and the *Anti-Money Laundering and Counter-Terrorism Financing Rules Instrument 2007 (No. 1)* (Cth) (Rules) require reform.

COBA has undertaken consultation with its members to obtain their views of the potential benefits and impacts that the proposed reforms to the AML/CTF regime will have across the membership. The proposed reforms have been considered by COBA and its members holistically in terms of both short- and longer-term implications and with consideration to potential implications for systems and technology, data, processes, people, governance, and oversight.

Consolidated feedback from our members regarding Part 1 of the Consultation Paper, *Simplifying and modernising the regime*, is under Appendix A. In relation to Part 2 of the Consultation Paper, *Tranche-two entities*, COBA supports the Tranche-two reforms to regulate designated non-financial businesses and professions (DNFBPs) under the AML/CTF regime as it will more closely align Australia with the international standards as stipulated by the Financial Action Task Force (FATF).[1] COBA believes that the Tranche-two reforms will:

- Reduce the risks of money laundering and terrorism funding in Australia.
- Close a significant gap in Australia's AML/CTF regime.
- Relieve some of the regulatory burden on current REs, who could rely on customer due diligence conducted by DNFBPs.

COBA filed a submission with the Criminal Justice Policy and Programme Division at the AGD on 31 January 2017 confirming support for Tranche-two entities to be brought under the AML/CTF regime and our position remains unchanged.

COBA notes that the consultation paper states that "AUSTRAC is considering various options to ensure that any future funding model is applied appropriately to existing and newly regulated entities under the enhanced regime". Given the potential impact on our sector, COBA would like to be included in any future consultations on the AUSTRAC funding model.

Additionally, COBA welcomed the briefing held with Dan Mossop (National Manager Reform and Mutual Evaluation), Evan Gallagher (Principal Specialist – Policy) and yourself on 6 June 2023. The conversation was insightful and allowed COBA to clarify the proposed provisions that would have the greatest impact on its members.

This submission elaborates on the feedback presented by COBA in the briefing.

[1] FATF, *Anti-money laundering and counter-terrorist financing measures in Australia* (2015), 168.

Second round consultation

COBA understands that the second-round consultation will be informed by the industry submissions from the first round of consultation and is due to commence in September 2023. To better position our members to evaluate the potential impacts of the proposed AML/CTF reforms, we look forward to seeing the proposed next steps and indicative timeframes with respect to the AML/CTF reforms.

We look forward to further conversations in relation to our submission and we thank you for taking our views into account. Please do not hesitate to contact Leanne Vale, Director Financial Crimes and Cyber Resilience (lvale@coba.asn.au) if you have any questions.

Yours sincerely

MICHAEL LAWRENCE
Chief Executive Officer

Appendix A: COBA Comments on Simplifying and Modernising the Operation of the Regime

Number	Question	COBA Comment
Streamlining Part A and Part B into a single program		
1	How can the AML/CTF regime be modernised to assist regulated entities address their money laundering and terrorism financing risks?	**Streamlining Part A and Part B into a single program** COBA does not support streamlining Part A and Part B into a single program as currently proposed as it is likely to lead to additional governance and oversight complexities for our members. We strongly encourage AGD to consider any potential adverse governance and operational impacts that could occur from streamlining Part A and Part B into a single program. For instance, the proposed structure of a single program will require Board and senior management oversight and approval of Part B obligations which have not historically been part of their AML/CTF Program endorsement and oversight responsibilities. The current Part B program and its specific compliance obligations are highly technical with respect to Know Your Customer (KYC)/Customer Due Diligence (CDD) obligations. COBA is concerned that our members' Boards and senior management will acquire additional burdens so as to understand these technicalities and to meet continuous oversight responsibilities. For example, this would include having regular reporting to the Board and senior management and attestations from their AML/CTF Compliance Officer (AMLCO) and compliance teams as to the efficacy of KYC/CDD practices. We believe that it would be appropriate that a revised governance structure for Part B obligations be adopted so that the Board has a high-level oversight of the risk environment, with the responsibility and approval of the technical operation sitting under senior management. It is also likely that streamlining Part A and Part B into a single program will increase the scope for Independent Reviews (IR). This will result in significant additional cost and effort for our members to undertake assurance activities with respect to the IR obligations. **Remove complexity and promote greater certainty** The current AML/CTF legislation is overly complex and the proposed reform agenda provides an important strategic opportunity to achieve greater certainty and tangible outcomes from Australia's AML/CTF regime. COBA recommends that there is careful consideration and definition be made by the AGD of the hierarchy of the Act, Rules, and AUSTRAC guidance. A clear legislative hierarchy and clear allocation of responsibility between differing instruments will assist REs to better understand the regulator's interpretation of the legislation and the expectations of REs.

Number	Question	COBA Comment
		It will also be critical for industry specific guidance to be produced, regularly updated, and made available to REs, as it will outline the minimum expectations in assessing and mitigating ML/TF risks as well as implementing prescribed controls. COBA welcomes AGD's and AUSTRAC's offer to collaborate on potential areas of sector specific guidance where COBA subject matter experts can help shape technical policy. On the importance of good legislative design and of maintaining clear legislative hierarchy and allocation of responsibility between instruments, COBA suggests for the AGD's consideration the Australian Law Reform Commission's expansive discussion on this topic in its *Financial Services Legislation Interim Report B* (ALRC Report 139, September 2022). **IFTI reporting** COBA members currently utilise third party suppliers to offer customers International Funds Transfer (IFTI's) facilities, for example, vertical internet banking integration with Western Union (Convera) or other similar money transfer providers. These suppliers submit IFTI reporting on behalf of COBA members as they are the reporting interposed entity under the 'first-in-last-out' rule under the current regime. COBA opposes any change to the current interposed routing entity reporting obligations as it would potentially see our members withdrawing these service offerings to customers.
2	What are your views on the proposal for an explicit obligation to assess and document money laundering and terrorism financing risks, and update this assessment on a regular basis?	COBA acknowledges that the current AML/CTF regime implicitly requires REs to conduct a ML/TF risk assessment as part of its AML/CTF Program. Moving to an explicit obligation to assess and document an REs ML/TF risk, will not materially impact our Members. However, COBA supports an AML/CTF regime that maintains risk-based regulation and emphasises the requirement to avoid undue prescription regarding procedures to satisfy this obligation. As such, there should be flexibility as part of any changes to the AML/CTF regime to take proper regard of the size, nature, and complexity of REs subject to its regulation. Further, explicit triggers to review the ML/TF risk assessment will challenge REs to demonstrate the minimum control requirements and in turn may impact resourcing as well as systems and controls that may require enhancement and/or implementation. COBA suggests that flexibility regarding timelines and trigger events be considered in this consultation process. Any greater degree of prescription and application of minimum standards will ultimately place an unfair burden on small financial institutions (FIs). For instance, COBA member banks that are small and regionally

Number	Question	COBA Comment
		based have different risk profiles compared to global FIs with complex product offerings and correspondent banking operations.
3	For currently regulated entities, to what extent do you expect that a simplified AML/CTF program obligation would affect your AML/CTF compliance costs?	**Systems and technology** A large proportion of COBA's members are currently undergoing substantial AML/CTF uplift projects covering areas such as system enhancement and resource uplift. This has resulted in significant monetary, time, and resource investment being made across the sector. Members are conscious that while investment has been made to date, the proposed AML/CTF reforms will likely require further system enhancements. Members have indicated that longer time horizons for implementation are needed to support future planning and to align with other major technology changes arising from policy reforms. The proposed reforms are expected to have a material impact on COBA members' current systems and technologies, requiring substantial investment to update/upgrade to accommodate the new obligations under the AML/CTF regime, especially where significant investment in system enhancements have already occurred. For instance, if the proposed AML/CTF reforms require an automated, real time tailored transaction monitoring program and/or there is prescription for more adaptive and real time customer risk assessment, this may require COBA's members to transition away from current systems and procure specialist third-party platforms, at significant cost. In addition, even minor system enhancement requests to customise existing third-party platforms, results in substantial costs with lengthy lead times. Currently, the AML/CTF Act, Rules, and AUSTRAC guidance are technologically agnostic. However, the direction of the proposed reforms and the subsequent minimum requirements suggest that some degree of systems and technology will be required to ensure compliance with the new AML/CTF regime. Many of COBA's members utilise third party providers which creates a concern that some providers will not have necessary capacity to deliver system enhancements if all REs are required to simultaneously implement changes. Further, the proposed reforms have the potential to place smaller REs at a competitive disadvantage as access to and ability to invest in technology and resources vary. It will impact how COBA's members can implement at pace, as well as compete with sophisticated solutions expected to be developed by larger REs. **Resourcing requirements** Similarly, it is anticipated that additional resources will be required to meet the proposed AML/CTF obligations, which will have further implications on costs. The introduction of regulation across Tranche-two

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		entities will place a high demand on an already constrained Australian talent pool of financial crime (FC) subject matter experts (SMEs) as well as place greater pressure on members to attract and retain this in-demand talent. Given there is a skill shortage in Australia for FC SMEs, it is going to place extreme pressure on COBA's members to undertake programs of the proposed changed AML/CTF obligations. COBA acknowledges that while it is generally supportive of the ALMCO role being at senior manager level, there needs to be consideration that smaller REs may not have the size and scale within their organisational structure to accommodate this requirement. Exemptions for smaller REs need to be considered to ensure the nominated AMLCO is at the right level with consideration of the REs size. COBA recommends that any obligations concerning the AMLCO be aligned with, or not contradict, the Banking Executive Accountability Regime (BEAR)/Financial Accountability Regime (FAR). COBA members are currently subject to the BEAR and will be subject to the FAR when it is passed by Parliament. The regimes impose accountability and governance obligations on the senior executives of regulated entities with a specific responsibility on the management of an ADI's anti-money laundering function. The AGD should consider this when developing the AMLCO provisions so as to not develop conflicting obligations on FIs that are subject to both the BEAR/FAR and the AML/CTF regimes. A final consideration is the unique operating model of COBA's members, which operate on a mutual model where the bank is owned by its customers rather than by shareholders. This limits COBA's members capacity and resources to pivot with changing regulatory compliance requirements. The nature and extent of the proposed AML/CTF reforms will likely absorb existing budgets and resources diverting resources from other development projects for the benefits of their customers such as new product offerings or new digital platforms. This will result in a limiting of our members' ability to provide competitive and attractive products to Australian customers in a market currently dominated by the oligopoly of the major banks. Large FIs will be able to leverage their competitive advantage through existing infrastructure, processes, and resources to effectively remain compliant to the new AML/CTF regime and simultaneously entrench their market dominance. This could drive a further wedge between large global FIs and COBA's members. As seen in the superannuation industry, implementation and compliance costs may be so substantial and disproportionate to size, that mergers and acquisitions may continue to occur throughout the industry further reducing competition and choice for customers in the Australian banking sector.

Number	Question	COBA Comment
Customer due diligence		
8	What are your views on the proposed simplification of the customer due diligence obligations as outlined?	COBA welcomes further clarification from AGD and AUSTRAC in the next round of consultation on what the proposed simplified CDD obligations will mean in practice. There is a view among our members that the proposed changes may reduce, or even remove, mechanisms currently available to REs to perform CDD. This would not be aligned with COBA's position of maintaining a risk-based approach in the AML/CTF regime. COBA's members also seek greater clarity as to when simplified CDD may still be applied under the new regime, including an early view on the types of circumstances under which it can still be applied. Based on the detailed discussions held with AGD and AUSTRAC on 6 June, COBA understands that international approaches will be considered for changes to the Australian simplified CDD regimes. COBA recommends that the United Kingdom's position should be considered as an appropriate model for adoption in Australia. Its equivalent to the simplified CDD regime includes consideration of factors such as: • The type of customer, product, transaction, and geographic location help to determine the circumstances under which simplified CDD may still be applied. • REs are required to identify and verify the customer's identity, but the level of scrutiny may be lower compared to standard CDD or Enhanced CDD (ECDD). • Transaction monitoring must occur continuously with unusual or suspicious activities identified and reported. • There are ongoing customer and transaction risk assessments. • Obligation to maintain adequate records so to demonstrate compliance with simplified CDD requirements. • The requirement for regulatory oversight. COBA would be generally supportive of Australia's simplified CDD requirements following the UK's provisions noting that AGD and AUSTRAC should also consider that the product structure and operability for mutuals (i.e., building societies) in the UK may differ. **Removal of safe harbour provisions** Many of COBA's smaller members rely on safe harbour provisions to undertake simplified CDD for customers determined to be low-risk, and, therefore, the removal of this provision will impact on their systems, processes, and resourcing requirements. It will also likely result in a complete redesign of COBA's smaller member's onboarding processes, which may negatively impact on customer experience, especially in the digital space. This includes both manual onboarding processes and any supporting technology.

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		Removing the safe harbour provisions does not acknowledge the differences in risk profiles, organisational size, product, and customer segments across REs, including within the customer owned banking sector. Risk-based exemption mechanisms that consider these factors as well as the operation and location of the business need to be considered. Especially as many of COBA's members are small regional REs with their customer composition generally of lower risk compared to larger regional and major banks. COBA looks forward to the next round of consultation to understand whether any changes would impact on the ability to apply CDD on vulnerable persons or marginalised individuals. Especially for victims of domestic violence and for indigenous communities, who may not have sufficient identification documents. **Systems and technology** In relation to systems and technology, COBA would like to see clarification in the next stage of the consultation process regarding the following as it relates to simplified CDD: • Trigger events that would require customer information to be updated and re-verified. • Expectations of a tailored Transaction Monitoring Program. The proposed AML/CTF reforms, will likely require significant uplifts to COBA member's onboarding, Ongoing CDD (OCDD), and ECDD systems and platforms. COBA's members utilise a number of third-party providers in relation to outsourcing key OCDD and ECDD activities and have reservations regarding the available capacity of these vendors to deliver customised system enhancements in a timely manner. **Privacy Act 1988 (Cth)** COBA's members seek clarification regarding the intersection of the proposed AML/CTF reforms in light of the current *Privacy Act 1988* (Cth) (Privacy Act) review. Consideration must be afforded to the following aspects: • Retainment of records for a specified length of time. • Data breaches involving significant amounts of Personal Identifiable Information (PII) (for example, client onboarding information). Considering recent data breaches across a range of industries and sectors, COBA is observing that customers are hesitant and frustrated by the volume of PII being captured, retained, and updated under the current AML/CTF regime. Given this, COBA encourages AGD to consider a strategy regarding digital

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		identification as a part of the KYC provisions. An example of this issue is the unclear acceptance and validation of digital drivers licences and proof of age cards in various states. **De-risking and offboarding of high-risk customers** In recent years, some FIs have declined, withdrawn or limited banking services to customers in certain industry sectors due to factors such as commercial considerations, reputational risk, and regulatory risk exposure.[2] In these situations, many inherently high-risk industries and customers turn to COBA's members for services "as a last resort". COBA's members are concerned that the proposed AML/CTF reforms will drive further de-banking by the major FIs, and that this trend will continue with a risk of displacement of high-risk customers from larger to smaller banks. **Beneficial Ownership register** COBA strongly encourages the establishment of a Beneficial Ownership (BO) register as it will create a single repository of company ownership. However, our support is conditional in that the BO register must not unintentionally capture COBA's members. Especially as their mutual structure, which provides each customer with the same share of ownership, prevents a single customer from gaining a controlling interest. Requiring the public listing of the customers of our members would be a significant breach of their privacy. COBA is happy to share our submission to Treasury on its 2022 consultation on the beneficial ownership register with the AGD and AUSTRAC if it is of assistance on this matter.

[2] AUSTRAC, *Financial services for customers that financial institutions assess to be higher risk* (7 June 2023).

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Amending the tipping-off offence		
11	Are there aspects of the tipping-off offence that prevent you from exchanging information, which would assist in managing your risks?	FATF guidance released in 2017 on private sector information sharing expressed that "effective information sharing is one of the cornerstones of a well-functioning AML/CTF framework".[3] Allowing for greater private-private information sharing among REs will enable effective management and more rapid sharing of information in relation to identity fraud or scams against customers. COBA believes that the quality of Suspicious Matter Reports (SMRs) will increase if private-private information sharing is enabled outside of a Designated Business Group (DBG). Under the current AML/CTF regime, the penalty for breaching the tipping off offence is imprisonment for two years,[4] which, understandably, causes REs to take an overly conservative approach to sharing information. The process of mergers and time taken to merge businesses is currently frustrated by DBG provisions not applying or not able to be granted in time once new legal entities are established. COBA supports the review of the tipping-off offence and encourages AGD to undertake a balanced approach to ensure an effective outcomes-based approach is adopted. COBA supports in principle a similar model to that of the UK.
Modernising the travel rule obligations		
17	Would the proposed model assist in addressing these [existing travel rule obligations] challenges?	While the proposed model would bring the travel rule in line with FATF Standards, COBA strongly encourages greater consultation with industry and consideration in respect to the acquisition and exchange of payee information. Practically, COBA questions whether the proposed travel rule model is possible in the current environment. The proposed reforms to the travel rule will have broad impacts on the banking industry in relation to the operating framework on domestic payments and transfer infrastructure. Additionally, to capture and retain additional PII raises concern for the interaction of the proposed AML/CTF reforms with the Privacy Act. However, COBA supports the travel rule aligning to the New Payment Platform (NPP) framework and the Reserve Bank of Australia's roadmap for payments, where possible. The current capture of additional identifiers within the transaction payment message needs further investigation with relevant stakeholders.

[3] FATF, *Private Sector Information Sharing*, (2017), 2.

[4] *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth), s 123(11).

Number	Question	COBA Comment
		COBA's members are concerned regarding the proposed travel rule model, with one member, whose customers are from defence and law enforcement occupations and as such disclosure could pose increased risk, stating the following: "*We are strongly opposed to the proposed model, payee information contains PII that should not be sent to another party without adequate controls for the sender to manage risk associated with its storage and use. Payee information has already been verified by the sending institution and should not be included as default behaviour, only as an exception in the context of an investigation by the receiving institution. Furthermore, as a receiving institution we are uninterested and unwilling to receive unsolicited PII from the sending institution and hence be responsible for its safe storage, management and timely deletion.*" Further, COBA's members highlight that the level of detail required to be compliant with this proposed model cannot be captured and retained on existing infrastructure, nor fed through transaction monitoring systems. Clarification of the level of detail to be obtained is required so to assess systems and technology capability and evaluate whether enhancements are needed to remain compliant. COBA also welcomes clarification on the reporting requirements of the travel rule, noting the proposed model is currently silent on these.