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Discussion Paper – Cost Recovery
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DISCUSSION PAPER: COST RECOVERY FOR AUSTRAC'S REGULATORY FUNCTIONS

The Association of Superannuation Funds of Australia (ASFA) would like to provide the comments below in relation to the Australian Transaction Reports and Analysis Centre's (AUSTRAC) discussion paper on the proposes AUSTRAC supervisory levy. The submission is in two parts: comments on the proposal to impose a supervisory levy, and comments on the proposed levy arrangements.

About ASFA

The Association of Superannuation Funds of Australia (ASFA) is a non-profit, non-political national organisation whose mission is to protect, promote and advance the interests of Australia's superannuation funds, their trustees and their members. We focus on the issues that affect the entire superannuation industry. Our membership, which includes corporate, public sector, industry and retail superannuation funds, plus self managed superannuation funds and small APRA funds through its service provider membership, represent over 90% of the 12 million Australians with superannuation.

Comments on the proposal to impose a supervisory levy

In the 2010 budget, the Australian Government announced its intention that AUSTRAC recover the cost of regulation from reporting entities.

The Association of Superannuation Funds of Australia is strongly opposed to the proposal.

ASFA would like to note at the outset that we are not aware of other jurisdictions which impose a similar cost recovery regime on regulated entities in relation to AML. The United Kingdom (UK) comes closest to the proposed regime as they impose some cost recovery on regulated entities. However regulation of AML in the UK is tied up in broader financial services regulation, so it is arguable that cost recovery for regulation in the UK is not directly related to AML regulation.

On the Australian proposal, the discussion paper notes that the Department of Finance and Deregulation's Australian Government Cost Recovery Guidelines require agencies providing government goods and services to the private and other non government sectors of the economy to recover all the costs of such products and services where it is efficient to do so. In the case of regulatory activities, the guidelines require that the individual groups that have created the need for regulation should bear the cost of that regulation. The paper goes on to state that the need for regulation by AUSTRAC arises because entities provide services that are vulnerable to exploitation for money laundering and terrorism financing purposes.

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ASFA disagrees with this view on two grounds.

First and foremost, the Government's 2003 announcement of a review of Australia's AML/CTF system was part of the implementation of revised international standards issued by the Financial Action Taskforce on Money laundering (FATF). The FATF is an inter-governmental body tasked with setting international standards and promoting policies to combat money laundering and terrorist financing.

Following consultations with stakeholders the Australian AML/CTF system was designed around a narrow group of Reporting Entities conducting identity checks on customers and reporting a range of financial transactions and suspicious behaviours to AUSTRAC.

Prior to settling on the final package of reforms to strengthen Australia's AML/CTF system the FATF *Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism* which evaluated the AML/CTF measures in place in Australia and identified strengths and weaknesses in Australia's system. The final design was, at least in part, in response to issues raised this report.

In effect, the Australian AML/CTF regime was the government's response to an international obligation. It was not because of a perceived need to, or public demand for, a change to the existing transactions reporting system. That is the need for regulation by AUSTRAC did not arise because entities provide services that are vulnerable to exploitation for money laundering and terrorism financing purposes. Rather the need for the enhanced regulatory regime was created by FATF and a perceived need to meet international obligations.

Significantly, the design of the Australian AML/CTF regime has taken the approach of regulating those bodies that are both easily regulated and where regulation produces the greatest effect for the least cost to the economy. Through their active and diligent participation these reporting entities are assisting in the fight against crime. Is this a privilege they should be paying for?

Secondly, there is no evidence that AUSTRAC provides reporting entities with government goods and limited evidence that it provides reporting entities with services.

ASFA does however note that the discussion paper posits that reporting entities obtain the following benefits through being regulated by AUSTRAC:

- A reduction in the risk that the reporting entity will be used for money laundering or terrorism financing purposes, and

- To the extent that reporting entities operate internationally, they obtain a benefit from operating in a jurisdiction that complies with the requirements of the Financial Action Task Force.

It is arguable that, absent their current AML/CTF obligations, reporting entities are ambivalent as to whether they are used for money laundering or terrorism financing.

In the superannuation context it is worth considering the respective roles of the industry's regulators; APRA, ASIC, the ATO and AUSTRAC.

APRA An APRA regulated superannuation fund pays APRA a significant licensing fee to begin operations and a significant annual levy based on the funds under management. APRA recovers from the industry the cost of regulating the industry. In return, superannuation funds are able to accept mandated Superannuation Guarantee contributions from employers and offer a range of superannuation products that are subject to concessional taxation arrangements. Part of the APRA levy is also used to fund the

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Superannuation Complaints Tribunal, some ASIC consumer work in the superannuation space and the ATO's Lost Member Register.

ASIC Should a superannuation fund wish to offer financial advice to members and others they are required to pay a small licensing fee to ASIC, and each year pay a fee when lodging their financial and other statements. In return for this fee the licensee is permitted to run a business of providing financial advice.

ATO The ATO administers laws that require superannuation funds to conduct their business in a specific manner. Additionally certain laws require superannuation funds to provide extensive amounts of data (information) to the ATO. This information is used by the ATO in the administration of the laws, including detecting breaches of law by superannuation fund members. The information provided by the funds to the ATO comes at significant cost, but the ATO does not charge the industry a fee for the costs associated with receiving and processing the information. However, as noted above, a small part of the APRA levy is paid to the ATO for their administration of the Lost Members Register – a register that enables a superannuation fund member who has lost contact with their fund to locate their benefit and re-establish that contact. This is a service to funds and their members.

AUSTRAC AUSTRAC administers the AML/CTF laws which all non-SMSF superannuation funds are required to comply with. Funds incur significant ongoing compliance costs with regard to these laws and undertake activities in excess of those required for normal business operations. Where required, funds also submit specific reports.

ASFA would argue that the work which the superannuation industry does, at significant cost, for both the ATO and AUSTRAC is similar in nature. It reduces the administrative and compliance burdens on those organisations and facilitates their meeting the government's objectives in a cost effective manner. ASFA would also like to note the significant costs entities have incurred in implementing AML/CTF compliance programs. The figure provided by one entity is $3 million.

ASFA considers that the proposal for cost recovery of AUSTRAC's regulatory function is akin to the ATO charging taxpayers a fee for lodging their tax return.

We note the dual role of AUSTRAC as the AML/CTF regulator and financial intelligence unit (FIU). There is no information provided in the discussion paper as to the financial contributions made to AUSTRAC by 'its partner agencies'. In the absence of further information it would appear that the suppliers of information (the reporting entities are subsidising the cost of delivering a service (financial intelligence) to the ultimate users of the information, AUSTRAC's partner agencies.

In conclusion, ASFA considers that the work of AUSTRAC provides a benefit to the whole of the Australian community. While it provides no specific benefit to the reporting entities, it is those reporting entities that are currently bearing a significant proportion of the total costs of Australia's anti-money laundering and counter-terrorism financing program.

Comments on the proposed levy arrangements

Section 2 of the paper sets out the cost elements that AUSTRAC intends to recover through the levy. One element of this is a component to support better AML/CTF compliance outcomes among small business. It would appear that this cost has been included in the base component, which is payable by all reporting entities. Earlier in the document it was stated that, in case of regulatory activities, the guidelines require that the individual groups that have created the need for regulation should bear the cost of that regulation. However, in this instance the basic levy structure ensures that all or a part of this cost will be

born by entities that are not 'small business'. It appears to be a clear case of extracting the money from those who can afford to pay – large entities.

The large entity component will apply to reporting entities with more than 150 full-time equivalent (FTE) staff. It is noted that in a designated business group each entity will be separately levied. This will create some anomalous, and some would say unfair, outcomes. ASFA is aware of financial services companies where the vast majority of employees are employed by one entity, but other financial service companies where there are several related entities which also have their own employees. Many of these related entities would have in excess of 150 employees. One organisation has estimated that, based on the figures provided in the discussion paper, its levy will exceed $50,000 in the first year.

Each entity will pay a base levy and those with more than 150 employees will also pay the large entity component. Thus two designated business groups could have the same number of overall employees but pay significantly different levy amounts depending on how they were structured. Clarification will be required as to how admissions and removals from the designated business group throughout the year will be handled.

In the superannuation sector the method of levying the fee based on FTE will also produce some odd outcomes.

For AML/CTF purposes the reporting entity is the entity that provides the designated service. Within the superannuation sphere those services are provided by either the fund itself (Section 6, Table 1, items 40 and 41 uses the term 'provider') or the trustee of the fund (Section 6, Table 1, items 42 and 43 uses the term 'trustee'). However a trustee of a superannuation fund is entitled to be indemnified out of the corpus of the superannuation trust for costs incurred in carrying out its duties as trustee. This means that the AUSTRAC levy in respect of both the superannuation trust and its trustee's obligations will be paid for out of the corpus of the superannuation trust. That is, by the members of the superannuation fund.

To avoid this dual levy situation ASFA suggests that as part of the legislative arrangements, the wording of Items 40, 41, 42 and 43 be revised to achieve consistency. As a superannuation fund can do nothing by itself, but can only operate through its trustee, it would appear logical to reword Items 40 and 41 in terms similar to Items 42 and 43.

For superannuation funds, what the actual cost impact will be will depend, under current proposals, on the structure of the administration arrangements. Some funds are self administered while others are externally administered and yet others are administered by a professional trustee. As such, the number of staff employed by funds and trustees, the reporting entities, will vary greatly. ASFA is aware of a superannuation fund with in excess of $10 billion of funds under management that employs fewer than 20 staff, as does its trustee, as all functions are outsourced. This fund and its trustee would each only be liable to the base component. Thus, within the superannuation industry, the situation will arise where there will be two superannuation funds of the same size in terms of funds under management who will pay entirely different levy amounts.

This inconsistent outcome is not satisfactory and consideration should be given to a more equitable method of determining the levy.

Yet another anomalous situation is that of superannuation fund administrators who provide a service of administration of superannuation funds' AML/CTF requirements. A case in point is that of a superannuation fund administrator that holds an Australian Financial Services Licence so that it can arrange for and undertake the necessary administration activities for superannuation fund members to receive the following designated services:

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- Item 40 – accepting the purchase price of a pension;
- Item 41 – making payments by way of pension or the commutation of pensions;
- Item 42 – accepting superannuation contributions, rollovers or transfers of benefits;
- Item 43 - payment of the whole or part of a superannuation benefit

The administrator is captured as an AML/CTF reporting entity because it provides a designated service under Item 54 of Table 1 in section 6 of the AML/CTF Act.

These administration companies are large organisations, typically employing many more than 150 staff. As such they will be liable for both the *base component* and the *large entity component* of the AUSTRAC supervisory levy. However, it is the superannuation fund that is the **provider** of these designated services, not the administrator, and it is the superannuation fund that is required to submit reports, such as suspicious matter reports and compliance reports, to AUSTRAC.

As these administrators provide only Item 54 services they have reduced obligations under the AML/CTF Act regarding customer identification and record keeping, an exemption from lodging AML/CTF Compliance Reports and the application of a Part B AML/CTF Program only. That such an entity should be required to pay a *large entity component* is inconsistent with the stated reason for the large entity component: "that it relates to additional expenses incurred by AUSTRAC in regulating large entities". Further, the statement that "larger entities have relatively more customers and typically provide products that are more complex over multiple distribution channels and multiple jurisdictions" is certainly not applicable to a pure administration company.

In light of these reduced obligations, and that reduced obligations apply to entities when only providing item 54 services, the application of the large entity component is seen as being inappropriate.

ASFA considers that, as a minimum, reporting entities whose only services are item 54 services should be exempt from the large entity component.

ASFA notes that AUSTRAC will apply the levy once annually and the levy will relate to the projected costs incurred by AUSTRAC for the year in which the levy is invoiced and collected. Whilst this is similar to the method used by APRA, in the first year it will make it difficult for reporting entities to budget appropriately. AUSTRAC will not be able to calculate the levy until the first census is complete. This creates great uncertainty around what the actual levy amount will be. Given this, ASFA requests that consideration be given to having a significantly later payment date for the first year.

ASFA cautions on AUSTRAC using current registration records as a basis for estimating proposed levies. We are aware of many financial advice entities which, though registered with AUSTRAC, are not technically required to do so as they do not have a compliance report obligation.

ASFA members have raised concerns with the table on Page 8. Specifically, clarification is sought on what is meant by 'managed investment trustees'. There is also concern about how reporting entities will be classified for the purposes of the transaction report component of the levy. What report volumes are being measured? Is it threshold transaction reports international financial transaction reports, suspicious matter reports etc?

While table 3.1 also mentions super fund trustees, financial planners and insurance product issuers, the vast majority of these entities would have no transaction reporting obligations. ASFA would like clarification that report volumes do not include suspicious matter reports. The concern is that these are

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provided to help law enforcement activities and that imposing a levy on these may result in an under-reporting of these matters, a less than desirable outcome.

In summary, ASFA is concerned with both the proposal to impose a levy and the method of calculation of the levy:

- The AML/CTF legislation imposes a huge cost impact on, but delivers no direct tangible benefits to, reporting entities.
- Australia's AML/CTF regime adopts a risk based approach and yet there is no consideration within the paper as to what are high risk and what are low risk sectors.
- The proposed levy arrangement of using FTE numbers does not appropriately reflect commercial business arrangements and will result in inequitable and anomalous outcomes.

If you have any questions or comments on this matter, please feel free to contact Robert Hodge, Principal Policy Adviser on 02 8079 0806 or by email rhodge@superannuation.asn.au.

Yours sincerely,

David Graus

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