

AUSTRAC on guard

Our AML/CTF watchdog has once again been kept busy keeping guard over compliance with new requirements, writes **James Cozens**

AUSTRAC, the body responsible for overseeing reporting entities' compliance with the *Anti-Money Laundering and Counter-Terrorism (AML/CTF) Financing Act 2006*, has again been busy throughout November. The regulator's newly appointed CEO, John Schmidt, has certainly been playing the role of tough cop ever since his appointment in September this year.

Little Persia, a small Parramatta remittance service provider, was hit with a remedial direction at the beginning of November with Schmidt re-emphasising that "the purpose of having an AML/CTF program is to identify, mitigate and manage the money laundering and terrorism financing risk a reporting entity may face".

Then there was the very recent announcement that AUSTRAC had carried out an assessment of PayPal Australia's AML/CTF program which revealed deficiencies in the systems PayPal had in place to assess and manage its money laundering and terrorism financing risk.

These recent AUSTRAC enforcements follow the July actions against Barclays Bank PLC and Mega ICBC and, while enforcement actions have targeted both the smaller and

larger business types, the messages are still the same: AUSTRAC is keen to show that it is serious about protecting the integrity of the Australian financial system; and all undertakings point back to a general failure in risk management.

Increased surveillance

The regulator's 2009-10 Supervision Strategy specifically outlines their intention to increase surveillance of the estimated 18,000 reporting entities that are required to comply with the *AML/CTF Act* and Rules.

Many entities will already have experienced the increasingly popular AUSTRAC desk review. Further, on-site assessments conducted by the regulator have increased by 47 per cent this year.

As the Little Persia direction has perhaps intentionally highlighted, eventually your AML/CTF program will be assessed regardless of your size and you need to be comfortable that it is robust enough to meet the obligations that are imposed upon your business by the *AML/CTF Act* and Rules. The one clear message to any reporting entity is simple: adequately address the risk management aspects of your program design or face costly and potentially damaging enforcement actions.

Practical steps

So, what lessons can be learned from this case, and what should the AML/CTF compliance officer be doing to make sure that they have adequately addressed the obligations imposed upon them by the *AML/CTF Act*? The key to any successful program is twofold: a structured risk assessment and the direct application of your program into your business.

It is clear from experience that the risk assessment of a reporting entity's delivery methods, customer types, foreign jurisdictions and designated services is the area in which most entities are falling short. More worryingly – though perhaps not surprisingly – is that this problem is just as prevalent in larger reporting entities, such as large multinational investment banks, as it is in smaller reporting entities who do not share similar resources, or the experience, of these global reporting entities, such as Barclays or PayPal.

The AUSTRAC Guidance Note, *Risk Management and AML/CTF Programs*, sets out in some detail the regulator's expectations with respect to the implementation of a risk management program for AML/CTF purposes. In particular it notes that:

- AUSTRAC would expect a reporting entity's risk management framework to deal with the following two categories of risk:
 - (a) Regulatory risk – that is, risks associated with the breaches of the relevant provisions of the *AML/CTF Act* and Rules, and
 - (b) Business risk – that is, the risk that designated services may be used to facilitate money laundering or terrorism financing.

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- AUSTRAC also expects reporting entities to develop and maintain logical, comprehensive and systematic methods to address:
 - (a) Risk identification and assessment – including the assessment of the likelihood and impact of the risk event taking place and the overall level of risk; and
 - (b) Risk mitigation and control procedures – relevant to the level of risk identified.

While not prescribing any specific risk management methodology, the AUSTRAC guidance note references the Australian Risk Management Standard AS/NZS 4360:2004, which should be referenced when undertaking your risk assessments. There is also a useful guidance note which is available on the AUSTRAC website, “Risk Management: A tool for small-to-medium sized businesses” and this provides some more practical guidance in this area.

The second part of a successful program involves the direct application of your AML/CTF program into your business. The importance of

drafting a unique program which is designed around the designated services that your business provides is critical, and this was highlighted in the Barclays enforceable undertaking, as well as, to some extent, PayPal.

There are numerous service providers out there offering template AML/CTF programs which, without tailored application, are ineffective. Reporting entities are offered AML “solutions” which are really just template documents. Reliance on these templates by any AML/CTF officer can be extremely dangerous.

However, by following the steps contained within the AS/NZ 4360 standard, and then directly applying your risk assessments back to your specific business activities, this process can be relatively straightforward.

Second tranche?

Tranche II of the *Anti-Money Laundering and Counter Terrorism Financing Act 2006*, which could bring lawyers, accountants, real estate agents and jewellers within the AML/CTF regime, has been delayed by the Government and is now expected to be implemented some time in 2010.

The Minister for Home Affairs, Brendan O’Connor, did not take the opportunity to shed any light on the issue at the AFMA conference in November. Instead, he simply reiterated that the Government will make a decision on whether to proceed in December. AUSTRAC’s public position has always been that it can’t do anything until it receives direction from the Government as to if and when Tranche II will commence. However, when I recently questioned Schmidt on this matter he noted that he expects “a considerable phasing and consultative process as happened in the first round”.

AUSTRAC will expect that the estimated 40,000 businesses which are caught under Tranche II will be capable of implementing effective risk management and compliance programs. However, as already highlighted, this is an area that many existing reporting entities are failing to address. This is particularly concerning because these entities should be experienced in risk management and implementing internal control programs, but the evidence so far is unconvincing.

It will be interesting to see how as many as 40,000 predominantly small-and-medium sized businesses will cope with this new challenge. **R**



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