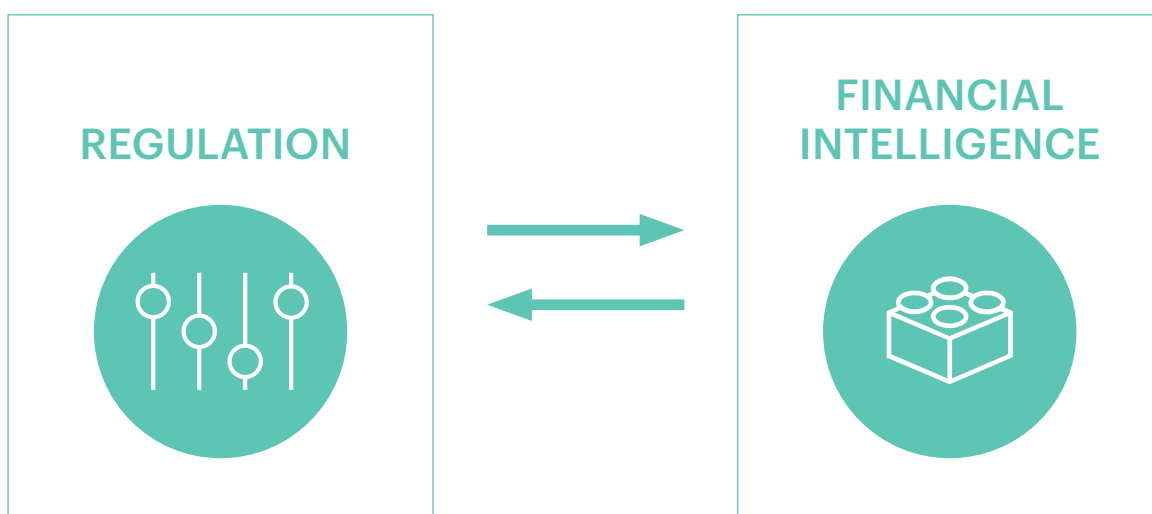


AUSTRAC'S APPROACH TO REGULATION

AUSTRAC's vision is a financial system free from criminal abuse. Our purpose is to build resilience in the financial system and use financial intelligence and regulation to disrupt money laundering, terrorism financing and other serious crime.

AUSTRAC's regulatory and financial intelligence functions are interconnected and complementary. AUSTRAC uses its knowledge of reporting entities, industry trends and money laundering and terrorism financing (ML/TF) risks to direct our regulatory efforts towards vulnerabilities and high-risk entities, which increases resilience to criminal abuse within the financial sector. Our regulatory work and engagement with reporting entities improves the volume and value of financial intelligence provided to partner agencies.



The *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (AML/CTF Act) provides the legal framework for AUSTRAC's regulatory function, describing the risk-based systems and controls that reporting entities are required to develop and maintain, as well as their reporting obligations.

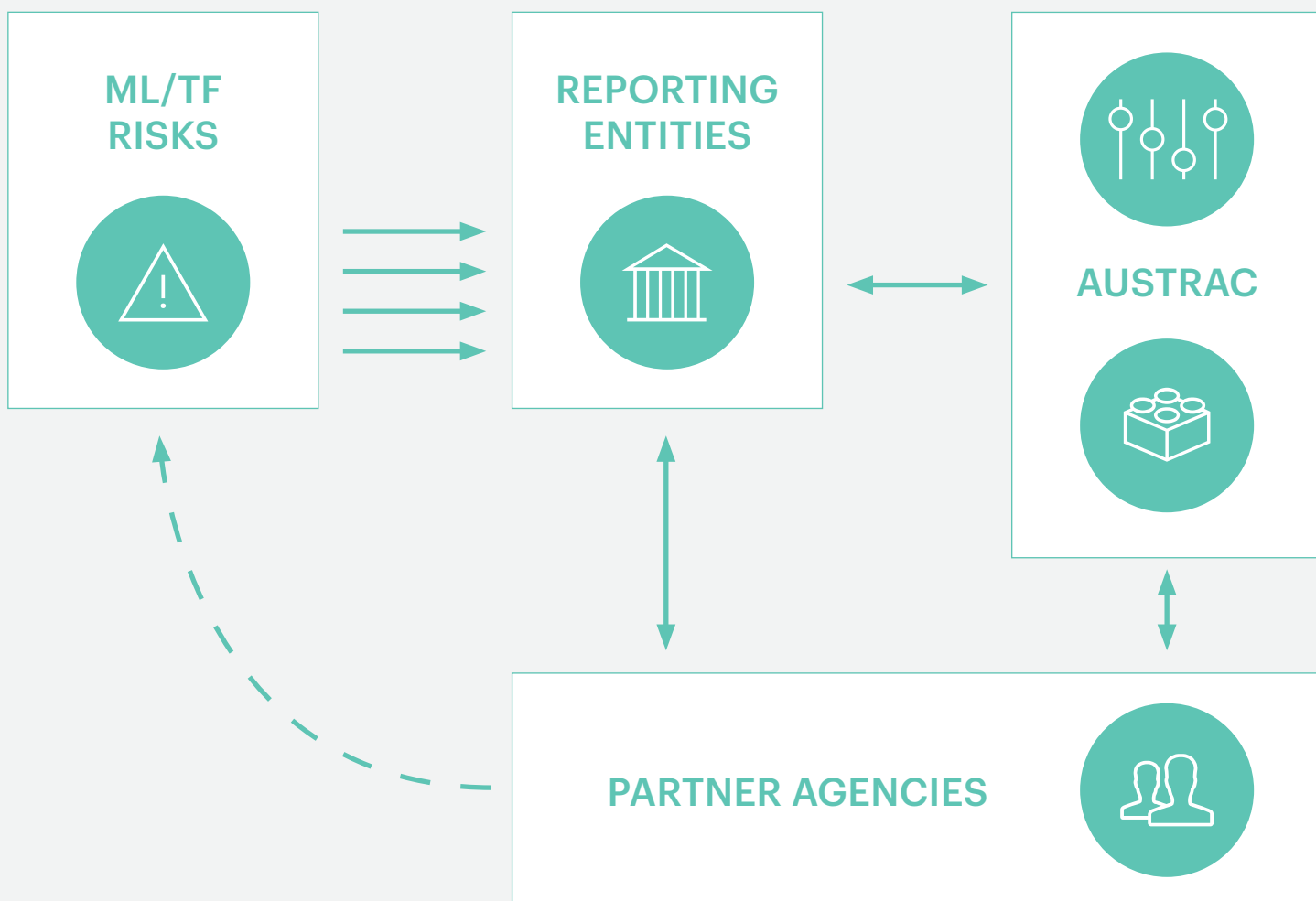
THE ROLE OF REPORTING ENTITIES IN AUSTRALIA'S AML/CTF REGIME

Australia's AML/CTF regulatory framework creates an important role for reporting entities in combatting and disrupting serious crime. Businesses are the first line of defence in protecting the financial system from criminal abuse.

The AML/CTF legal framework adopts a risk-based and principles-based approach to regulation and places the onus on reporting entities to identify, mitigate and manage their ML/TF risk. Reporting entities must have the necessary knowledge of their products, channels and customers to understand, respond to and report on the ML/TF risks they face. This reflects the degree of trust

Parliament has placed in industry for the operation of the AML/CTF risk management system.

AUSTRAC's approach to regulation recognises that reporting entities are our important partners. AUSTRAC, reporting entities and other government agencies, such as law enforcement and national security agencies, share a common interest in — and responsibility for — creating a financial system free from criminal abuse. Supporting, collaborating with and building the capability of the reporting entity population is critical to AUSTRAC achieving its purpose and vision.



AUSTRAC'S REGULATORY APPROACH AND PRINCIPLES

To realise its vision of a financial system free from criminal abuse, AUSTRAC works to ensure that regulated entities are knowledgeable, vigilant, and capable of preventing, detecting, and responding to threats of criminal abuse and exploitation.

Our overarching approach to regulation is to:

- **Simplify regulatory requirements and align them to reinforce regulatory outcomes** and allow reporting entities to focus on preventing, detecting, and responding to criminal activity.
- **Promote a culture of AML/CTF compliance and best practice risk management** across the regulated community, recognising that most entities want to meet their obligations and do their part to prevent, detect and respond to criminal misuse of their business, but may need assistance to do so.
- **Develop a comprehensive understanding of ML/TF risks and share this across the AML/CTF community** so that reporting entities are able to use the insights from our financial intelligence work to better manage their own ML/TF risks.
- **Engage with reporting entities who are at risk of not meeting their AML/CTF obligations or adequately managing their ML/TF risks** to understand the causes of the issues and support them to better meet their obligations in the future.
- **Apply a forceful and credible deterrent to serious and systemic non-compliance** to maintain public confidence in Australia's AML/CTF regulatory framework and financial system, prevent future non-compliance, and ensure that businesses which meet their AML/CTF obligations are not disadvantaged.
- **Work with other stakeholders globally—including law enforcement, other regulators, AML/CTF service providers, Fintel Alliance partners and academia**—because we recognise ML/TF is a complex problem that we can only solve through collaboration.

REGULATORY PRINCIPLES

Our regulatory approach is underpinned by our regulatory principles, which explain how we perform our functions, exercise our powers and engage with the regulated community. AUSTRAC is committed to being:

- **Collaborative** – we seek to partner and collaborate with reporting entities and other stakeholders in recognition of our shared interest in combatting serious crime.
- **Risk based and intelligence led** – we understand the importance of understanding the ML/TF risk environment and accordingly, our regulatory approach, initiatives and prioritisation are targeted and driven by our analytical and intelligence capabilities.
- **Outcome focussed** – we direct our efforts towards achieving our regulatory objectives rather than 'tick-a-box' compliance. Our priority is ensuring that reporting entities manage their ML/TF risks effectively through systems and controls tailored to their business, not prescribing every detail of their risk management approach.
- **Calibrated and credible** – we exercise our regulatory powers in a proportionate manner, and demonstrate a high level of professionalism in all our dealings with external stakeholders.
- **Efficient and effective** – we allocate our resources to effectively achieve our vision while minimising costs to business and the government.
- **Reflective** – we review and refine our regulatory approach over time, recognising that our model cannot be static and must evolve as our environment changes.

AUSTRAC'S RISK-BASED APPROACH FOR ENGAGING WITH REPORTING ENTITIES

The entities AUSTRAC regulates vary widely in nature, size and complexity. These factors form the basis of an entity's ML/TF risk. Reporting entities' commitment and capacity to identify, mitigate and manage their ML/TF risks also varies.

Accordingly, AUSTRAC employs a risk-based approach to regulation, ensuring that our resources are allocated to best manage ML/TF risks across the Australian financial system, and that our interactions with regulated entities are aligned to their needs and circumstances.

Reporting entities can expect their regulatory interactions with AUSTRAC to vary. This is based on our assessment of their ML/TF risk exposure and how well they are meeting their obligations and managing their ML/TF risks.

As part of this, AUSTRAC considers a range of internal and external inputs including an entity's transaction and suspicious matter reporting, their compliance history, and information from partner agencies and law enforcement about the entity, their customers and the broader threat environment within which the financial sector operates.

AUSTRAC's approach is dynamic—as a given entity's ML/TF risk exposure and risk management changes, we will vary the mix of regulatory activities in which we engage.

REGULATORY ACTIVITIES

To tailor our regulatory activities to the needs and circumstances of reporting entities, and to ensure our resources are effectively allocated, we group our activities according to their type and intensity. The broad types of activity we engage in are as follows:

- **Partner and collaborate** – activities that we undertake to bring together AUSTRAC, reporting entities and/or other members of the AML/CTF community to improve our understanding of ML/TF risks and work together to prevent, detect and disrupt serious crime.
- **Build and improve capability** – activities that we undertake to support reporting entities to meet their obligations, uplift their AML/CTF capability and identify and implement best practice approaches to the management of their ML/TF risks.
- **Assure and enforce** – activities that we undertake to gain confidence that reporting entities are meeting their obligations and managing their ML/TF risks effectively, and where they are not, compel them to do so or take enforcement action as appropriate.

We further categorise activities based on their intensity—the level of engagement between AUSTRAC and reporting entities, and the time and resource commitment required from both sides. For example, assurance activities range from lighter-touch desktop reviews through to in-depth compliance assessments.



ACTIVITY TYPE

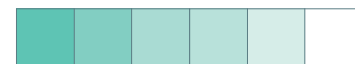
		PARTNER AND COLLABORATE	BUILD AND IMPROVE CAPABILITY	ASSURE AND ENFORCE
INTENSITY	HIGH	<ul style="list-style-type: none"> • Membership in the Fintel Alliance • Collaborating on joint projects (for example financial intelligence, policy and systems development) • Communities of practice • Meetings with senior executive and governance committees 	<ul style="list-style-type: none"> • Individualised advice on policy and operational issues • Participation in AUSTRAC-run training e.g. Financial Intelligence Analyst Course • Presentations to operational level staff to help them understand AUSTRAC's expectations • Regular meetings to reinforce opportunities to improve AML/CTF capability 	<ul style="list-style-type: none"> • In-depth compliance assessments (including on-site) • Remedial directions and enforceable undertakings • Monitoring of remediation programs • Enforcement investigations (civil or criminal) • Civil penalty proceedings
	MODERATE	<ul style="list-style-type: none"> • Providing feedback about reporting contribution • Facilitating forums to share information about ML/TF risks • Meet with industry bodies 	<ul style="list-style-type: none"> • One-to-one engagement (including on-site visits) with businesses with identified capability gaps • Targeted communications to businesses with identified capability gaps • Facilitating and attending industry forums and events 	<ul style="list-style-type: none"> • Use of administrative powers (e.g. cancellation of registration) • Requiring a reporting entity to conduct an ML/TF risk assessment or engage an external auditor to review its risk management or AML/CTF compliance • Infringement notices • Narrow but targeted compliance assessments (including on-site)
	LOW	<ul style="list-style-type: none"> • Publishing and disseminating timely information about ML/TF risks 	<ul style="list-style-type: none"> • Communications campaigns to improve business awareness of AML/CTF obligations • Development and publication of guidance and information material in collaboration with industry to help business meet AML/CTF obligations 	<ul style="list-style-type: none"> • Warning letters • Desktop compliance reviews • Monitoring of reporting entity activity

At any given time, we may engage in a range of the above activities based on a particular entity's ML/TF risk exposure and our assessment of how well they are meeting their obligations and managing their risks. The interaction between ML/TF risk exposure, AUSTRAC's degree of confidence and the activities we are likely to devote most of our effort and investment to is illustrated in the scenarios below. Our engagement model is not static and, as an entity and its environment changes, so too will their interactions with AUSTRAC.

EXAMPLE SCENARIOS

The colour coded boxes below illustrate how AUSTRAC might focus its efforts across the activity TYPE and INTENSITY options described on page 5.

KEY:

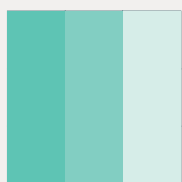


GREATER
FOCUS



LESS
FOCUS

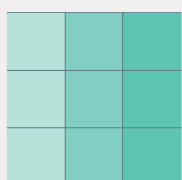
SCENARIO 1: BANK A LIMITED



SITUATION: We assess Major Bank A's ML/TF risk exposure as high, but we are confident that it is meeting its obligations and managing its risks effectively.

OUR APPROACH: Our engagement with Major Bank A will focus on collaborative and capability building activities. While we will undertake some assurance-oriented activities, these will be limited in number and have the main objective of ensuring that our evaluation of Major Bank A's ML/TF risk management remains correct.

SCENARIO 2: BANK B LIMITED

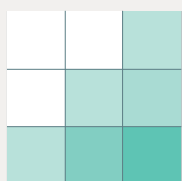


SITUATION: Major Bank B's ML/TF risk exposure is high and we are not confident that it is meeting its obligations or managing its risks effectively.

OUR APPROACH: Our engagement with Major Bank B will involve assurance/enforcement and capability building activities with the objective of reaching a state where we are confident that Major Bank B is effectively managing its ML/TF risks. If we identify serious or systemic non-compliance that remains unmitigated, we may consider taking formal enforcement action.

We will also seek to partner and collaborate with Major Bank B. This recognises that Major Bank B can still make a significant contribution to combatting serious crime and AUSTRAC will continue to work with them to do so.

SCENARIO 3: HOTEL C PTY LTD



SITUATION: Hotel C has a relatively low ML/TF risk exposure but we are not confident that it is meeting its obligations or managing those risks effectively.

OUR APPROACH: It is likely that most of our engagement with Hotel C will take the form of low intensity assurance activities and capability building activities with the objective of reaching a state where we are confident that Hotel C is effectively managing its ML/TF risks.

It is important to note that we may escalate the intensity of our assurance activities if Hotel C is not responsive to our concerns. In particular, we will not rule out formal enforcement action



EXERCISING AUSTRAC'S ENFORCEMENT POWERS

AUSTRAC's regulatory activities generally focus on working with reporting entities to increase their resilience to ML/TF risk and improve the quality of their reporting under the AML/CTF Act. AUSTRAC aims to achieve this by improving entities' understanding and capability in the area of ML/TF risk management and supporting their voluntary compliance with the AML/CTF Act.

However, because the consequences of poor AML/CTF systems and controls can be very serious, AUSTRAC may take enforcement action against a reporting entity for serious and/or systemic breaches of the AML/CTF Act.

In this section, we provide information about the factors AUSTRAC considers when deciding whether to take enforcement action against a reporting entity.

WHY AUSTRAC CONSIDERS ENFORCEMENT ACTION

Well-targeted and proportionate enforcement action benefits reporting entities and the wider community by contributing to the integrity of the financial system. AUSTRAC's enforcement activities are intended to:

- achieve current and future compliance at both the reporting entity level and the broader industry level through selective, targeted action
- deter non-compliance
- disrupt ML/TF activity taking place through reporting entities
- level the playing field for reporting entities who comply with their legal obligations
- communicate AUSTRAC's views about what constitutes unacceptable conduct to the financial sector.

HOW AUSTRAC SELECTS MATTERS FOR ENFORCEMENT

AUSTRAC may identify a reporting entity's failure to meet its AML/CTF obligations through its internal supervision or intelligence activities, voluntary disclosure by the entity, or referral of an issue of concern from a partner agency.

AUSTRAC's enforcement focus is on a reporting entity's serious and/or systemic non-compliance with the AML/CTF Act. We assess serious non-compliance in a range of ways including by analysing AUSTRAC data holdings, consulting with different teams within AUSTRAC, and requesting information from the reporting entity and partner agencies.

AUSTRAC has a range of investigative tools, including a broad power to issue a notice compelling production of information and/or documents relevant to the operation of the AML/CTF Act, Rules or Regulations (section 167 of the AML/CTF Act). Importantly, issuance of a 'section 167 notice' does not indicate an intention to take enforcement action—it is just one of the ways we ensure we have all the information needed to understand and assess potential compliance issues.

When considering whether enforcement action is the most appropriate response to identified non-compliance, AUSTRAC considers the circumstances of each case including:

- The nature of the non-compliance, such as the type and seriousness of the breach and whether it appears to be a systemic or isolated/one-off breach.
- The ML/TF risk associated with the reporting entity, including whether the entity's non-compliance has exposed itself and the financial system more broadly to significant risk of criminal abuse.
- The reporting entity's willingness and effort to comply, i.e. its compliance history, its level of engagement with AUSTRAC and its demonstrated efforts to identify, mitigate and manage its ML/TF risks.
- Whether the non-compliance was voluntarily reported by the reporting entity. Voluntary disclosure does not preclude formal enforcement action but is a factor we will consider. It may also be relevant to penalty if we do take formal action.
- The likely consequences of the enforcement action, for example the expected impact (remediation and deterrence) on both the individual entity involved and the broader reporting entity population.

In instances of minor and/or technical non-compliance that AUSTRAC considers do not warrant formal enforcement action, AUSTRAC works with reporting entities to enable them to appropriately respond and remediate issues in a timely fashion.

AUSTRAC applies governance frameworks to all decisions to commence enforcement action. Our decision-making process is rigorous and carefully considered.

Our objective is to ensure that ML/TF risks are effectively managed by the reporting entity. Where AUSTRAC has commenced formal enforcement action, we will strive to maintain an ongoing and positive relationship with the reporting entity—including continuing collaborative activities aimed at combatting serious crime, where appropriate.

ENFORCEMENT ACTIONS AVAILABLE TO AUSTRAC

AUSTRAC's formal enforcement action can include:

- Issuing an infringement notice.
- Issuing remedial directions, which require a reporting entity to take specified action to ensure compliance.
- Accepting an enforceable undertaking detailing the specific actions a reporting entity will commence or cease in order to comply with the AML/CTF Act. If the AUSTRAC CEO considers that a reporting entity has breached an enforceable undertaking the AUSTRAC CEO can apply to the Federal Court for orders requiring the reporting entity to comply with the undertaking.
- Seeking injunctions and/or civil penalty orders in the Federal Court.
- Referring a matter to the Commonwealth Director of Public Prosecutions for possible criminal prosecution.